

***DEFINITION AND RECOGNITION OF ELEMENTS OF ACCRUAL-
BASIS FINANCIAL STATEMENTS***

COMMENT LETTERS

AS OF AUGUST 29, 2006

**EXPOSURE DRAFT: *DEFINITION AND RECOGNITION OF ELEMENTS
OF ACCRUAL-BASIS FINANCIAL STATEMENTS***

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ATTACHMENT 1 – TEXT OF COMMENT LETTERS

#1 – Hal Steinberg, non-federal, other

June 27, 2006

Ms. Wendy Comes, Executive Director
Federal Accounting Standards Advisory Board
Suite 6814
441 G Street NW
Washington DC 20548

Dear Wendy,

I had a chance to read the Proposed Statement of Federal Financial Accounting Concepts on defining and recognizing elements in accrual-basis financial statements on the plane returning from the Association of Government Accountants conference in San Diego. Let me provide my comments while they are still fresh in my mind.

The proposed statement is thoughtful, well-written, and clear. Notwithstanding the positions the statement eventually takes, documents such as this can serve the Board well as a foundation for setting standards. My hats off to the persons who conceived of this approach to defining the elements and structured the document. You will note from my responses to the questions that I have little negative reactions.

RESPONSE TO QUESTIONS

Question 1. I agree that the definitions of assets and liabilities should derive from their fundamental or essential characteristics; the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities; and that an asset can meet the definition of an asset even if it is not measurable or is immaterial.. My one comment is that although “fundamental or essential characteristics” is not necessarily an accounting term, defining the term and explaining why it is important (either early in the document and/or in the Glossary) would facilitate understanding

Question 2. As for the first part of this question, I cannot think at this time of additional elements of accrual-basis financial statements that should be defined in the Concepts Statement. In fact, I like that the proposal has stated that gains and losses should be considered a subset of revenues and expenditures. I have often found distinguishing between gains and revenues or between losses and expenses to be contrived.

Regarding the second part of the question, it may be desirable and indeed necessary that additional elements be considered. There is no denying that the Federal Government has unique powers and responsibilities. There could be additional elements that do not readily fit in the five proposed elements. The reference in the question to stewardship assets, stewardship investments, and social obligations bears this out. I do not think it would be harmful for the concepts statement to acknowledge the possibility that because of the unique nature of the Federal Government, certain additional elements might need to be defined.

Question 3. A basic postulate of accounting is that financial statements are prepared as if the reporting entity is a going concern. Accordingly, the statements are based on existing and

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8/29/2006

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likely to occur conditions. Although the government can modify the law related to non-exchange transactions, the same as it can abrogate or renegotiate contracts, it would seem financial statements need to report present obligations after giving due consideration to the likelihood and amount of payment. This is similar to what is presently done with contingent liabilities.

Question 4. I believe the two fundamental and essential characteristics of a Federal Government asset are as good as any as I can think of at this time. I particularly like the way the power to tax is addressed.

Question 5. I believe the two fundamental and essential characteristics of a Federal Government liability are as good as any as I can think of at this time.

Question 6. I agree that the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived and the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

Question 7. I agree with the two conditions that should be met for an item to be recognized in the body of a financial statement. My only comment would be to ask whether the Board considered adding the probability of realization of the asset or liquidation of the liability as a third criteria in order to address the concerns of those that hold the alternative view.

Questions 8, 9, 10. I suspect considerable deliberation underlies the proposed concepts statement, and particularly the realization that for some aspects there are alternative views. While the proposed statement is fully written, it could not possibly capture all of the aspects and nuances of the alternative views. I feel it would be inappropriate to express a preference for one view or the other without having been a party to the extensive deliberations.

OTHER COMMENTS

Other comments I have from reading the proposed comments statement are as follows.

- Paragraph 31—I believe the explanation of control, as I understand it, could cause problems. I base this conclusion on two situations. First, if control of use and regulation of access is a determining factor for establishing an asset, then toll roads would be assets and toll-free roads would not. Second, as you know, there are natural resources to which the government has general access and which it sells, e. g., water rights, air waves. Failure to consider these resources as assets will result in the government receiving revenues from sales which it would have to classify as other than exchange revenue.
- Paragraph A10—The last sentence in this paragraph infers that a statement of financial accounting concepts would be revised to conform with a statement of financial accounting standards. I suspect this is not a situation the Board desires. It undoes the entire purpose of developing statements of financial accounting concepts in order to have a conceptual framework from which the standards can be developed.

It also, however, speaks to a current basic issue. The project related to social insurance is attempting to decide the manner in which this item should be reported. Considering that the Board recognizes the need to define the elements in accrual based Federal financial statements, it would seem premature to define how to report an item as large and as

different as social insurance prior to deciding the elements with which all items should be reported.

* * * * *

I hope this letter is helpful. Please feel free to contact me at any time to discuss its content or other aspects of the proposal, or for that matter, other issues the Board is considering.

Sincerely yours,

Hal Steinberg

#2 – Small Business Administration, Office of Inspector General, Sadie Lowe, Assistant Counsel to the Inspector General, Federal-Auditor

>>> "Lowe, Sadie L." <Sadie.Lowe@sba.gov> 6/28/2006 3:13 PM >>>

To Whom it May Concern:

The Small Business Administration, Office of Inspector General has reviewed this proposal; we do not have any comments.

Sincerely,
Sadie Lowe
Assistant Counsel to the
Inspector General
Small Business Administration
Office of Inspector General
Counsel Division
409 Third Street, SW
Washington, DC 20416
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202-481-6368 (f)

#3 – World Bank, Fayezul Choudhury, Vice President and Controller, Non-federal - Other

The World Bank
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

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U.S.A.

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Cable Address: INTBAFRAD
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June 29, 2006

David Mosso
Chairman, Federal Accounting Standards Advisory Board
441 S Street NW
Mailstop 6K17V
Washington, DC 20548

Dear Mr. Mosso

Thank you for your letter to Mr. Wolfowitz of June 13, 2006 seeking comments on the Board's Exposure Draft of a Proposed Statement of Federal Financial Accounting Concepts, Definition and Recognition of Elements of Accrual-Based Financial Statements.

As you may know, the constituent entities of the World Bank present financial statements in conformity with both private sector accounting principles generally accepted in the United States of America as well as with International Financial Reporting Standards. Accordingly, as a preparer of financial statements the World Bank does not have a direct interest in the conceptual issues raised in the Board's Exposure Draft that pertain to accrual-basis financial reporting by the U.S. federal government, and therefore we are not responding in detail to the Questions for Respondents.

However, the Bank does have a strong interest in strengthening the financial management performance of its client countries. Better accounting and auditing by governments in borrowing countries will contribute to improved development outcomes, as well as providing the Bank with greater assurance over the use of Bank funds. Accordingly, we support initiatives that can support our goal of building accounting and auditing capacity in developing countries: in this context, we commend the Board's leadership in developing a statement of concepts for federal financial reporting, that may be used as a model by countries other than the U.S.A.

You may be aware that the Bank has supported the activities of the International Public Sector Accounting Standards Board (IPSASB) for many years. The IPSASB is itself considering developing its own conceptual framework for financial reporting by governments. We would strongly encourage your Board to work as closely as possible with the IPSASB in developing the Statement of Proposed Federal Financial Accounting Concepts. It would be unfortunate – and confusing for the broader governmental accounting community around the world – if the two Boards were to reach different conclusions on substantive conceptual issues.

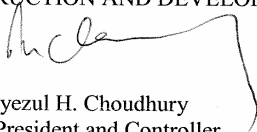
RCA 248423. ☐ WUI 64145 ☐ FAX (202) 477-6391

June 29, 2006

In the meantime, let me repeat the Bank's support for this important initiative, and to wish you luck with the exposure process, and subsequent finalization of the concepts statement.

Sincerely,

INTERNATIONAL BANK
FOR RECONSTRUCTION AND DEVELOPMENT



Fayeul H. Choudhury
Vice President and Controller

#4 – Scott Pirtle, Non-federal - Other

>>> "Scott Pirtle" <swp54@earthlink.net> 7/20/2006 11:59 AM >>>

To Whom It May Concern:

I am writing to show support of your ED concerning the above mentioned. As a citizen with children and grandchildren, I am very interested in seeing the government required to report all liabilities they have generated, or will generate in the future.

Thank you,

*Scott Pirtle
HorseShoe, NC*

#5 – Duncan McGhee, Non-federal - Other

>>> Athey McGhee <ourbuyacct@sbcglobal.net> 7/21/2006 4:32 PM >>>

To Whom It May Concern:

I am writing to show support of your Exposure Draft concerning the above mentioned (Definition and Recognition of Elements). I agree with the definition of liabilities as stated. As a citizen with children and grandchildren, I am very interested in seeing the government required to report all liabilities they have generated, or will generate in the future.

Thank you,

Duncan McGhee

Austin, Texas

**#6 – Social Security Administration Office of the Inspector General, Rona
Lawson, Director, Office of Audit, Federal - Auditor**

>>> "Lawson, Rona" <Rona.Lawson@ssa.gov> 7/25/2006 9:22 AM >>>

Wendy M. Comes

Executive Director

Federal Accounting Standards Advisory Board

The SSA Office of the Inspector General has reviewed the Exposure Draft - Definition and Recognition of Elements of Accrual-Basis Financial Statements. We have included our responses to the Questions for Respondents in the attached Word file. In addition, we have the following general comments on the Exposure Draft:

Paragraph 26 - An example is provided where equipment becomes "obsolete or unusable and has no scrap value" and therefore does not meet the definition of an asset. However, in paragraph 24, it seems to indicate that a machine that continues to provide a service may qualify as an asset even if there is no market for the machine. Since one of the definitions of "obsolete" is "superseded by something newer, though possibly still in use," we suggest deleting the word "obsolete" from paragraph 26 to avoid confusion.

Paragraph 53 - The definition of expense includes changes in accounts "from providing ...goods or services, or any other activity..." The same phrase, "from providing goods or services...or any other activity" is used in the definition of revenue as well. Consider changing "from providing" in the expense definition to another phrase such as "from the use of."

If you have any questions, please contact Victoria Vetter, Director, Financial Audit Division, at 410-966-9081.

Thank you for the opportunity to comment.

Rona Lawson

Director

SSA/OIG/Office of Audit

Attachment:

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

a) The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Yes. It makes sense that characteristics are taken into account when developing a definition.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Yes. These elements are based on what is done with or happens to assets and liabilities. Net position, revenues, and expenses all have a direct relationship with assets and liabilities.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Yes. We agree that there are some assets that are not recognized in the body of the financial statements. For example, we consider Social Security number cards to be Agency assets because the numbers are essential for economic functioning in our society. We also consider the databases maintained by SSA to be assets because the Agency has control and they provide benefit to the Agency, other agencies looking to verify information, and individuals.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues* and *expenses*. (See paragraphs 2, 3, 35-37, and 56.)
- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

At this time, we see no need for additional elements that should be defined in the Concepts Statement.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

At this time, we disagree that there are additional elements that need to be defined. However, as it relates to long-term social obligations, we believe that there is no liability beyond the benefits that are currently due and payable (the next month's benefit payment).

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have

occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page 29.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the position taken in the Alternative View. Paragraph 61 of the Concepts Statement, which is not part of the Alternative View, states that, "Measurement considerations also may result in postponing recognition of some assets or liabilities until their future outcomes become less uncertain or their measures become more reliable." Long-term social insurance benefits could be considered uncertain since there is on-going discussion regarding changes that are needed to the social security program and, as GAO has pointed out on numerous occasions, the program at its current benefit levels is unsustainable in the long-term.

- 4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Yes, we agree.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

No, we do not believe there are additional characteristics.

- 5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

We agree that these are the essential characteristics of federal government liabilities. There must be a present obligation to provide something of value and there must be an agreed or understood time of settlement.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?

No, we do not believe there are additional characteristics.

- 6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Yes, the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Yes, the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

No, there are no other criteria that we would recommend be established as conditions for recognition.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

We agree with the position taken in the Alternative View. Where items can be easily determined as meeting the definition of an element, a probability assessment may not be needed. However, for complex items, there is a need to assess the probability and to set a probability threshold so that items with a very low probability would not meet the definition of an element. For example, for social insurance, a probability assessment

should be completed. There are many factors that could change or influence the probability that a long-term social insurance liability exists.

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 26.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

We agree with the position taken in the Alternative View. We believe there would be instances where an assessment of probability would need to be made to determine if an item is measurable. Where items can be easily measured, a probability assessment may not be needed. However, for complex items, there is a need to assess the probability and to set a probability threshold so that items with a very low probability would not be considered measurable. For example, for social insurance, a probability assessment should be completed. To record a liability beyond what is currently due and payable, a detailed assessment would be required for what will be paid in the future. These payments are not readily known since there are many factors that could affect whether or not individuals ultimately receive benefits.

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page 27.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. We interpret SFFAC 1 to mean that overall the information in financial reports should have those qualitative characteristics. Some information by its nature may be difficult for readers to understand or may not seem relevant to them, but may in fact be required for complete financial reporting. Although the qualitative characteristics should be taken into account when making decisions as to what to include in financial statements, we do not believe those characteristics need to be repeated in this Concepts Statement. Nonetheless, it may be helpful to include some type of reference to SFFAC 1.

#7 – Environmental Protection Agency, Office of the CFO, Ofelia Moore, Acting Staff Director, Federal - Preparer

>>> <Moore.Ofelia@epamail.epa.gov> 7/26/2006 7:39 AM >>>

Dear Ms. Comes,

Thank you for providing us the opportunity to comment on the subject exposure draft. Here are EPA's comments:

1. There should be a clarification on liabilities that are contingent and probable, such as those reported in the Legal Representation Letter. Provide some clarifying examples.

2. In Paragraph 38, we recommend that the words "or, on demand" be eliminated from the end of the sentence so that the sentence reads as follows: "A liability is a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs."

With regards to the Questions for Respondents, EPA supports the responses that the CFOC Standardization Committee will submit to FASAB.

Sincerely,

Ofelia M. Moore, Acting Staff Director
Financial Policy and Planning Staff
Office of Financial Management
Office of the Chief Financial Officer
(202) 564-4943
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#8 – Immigration and Customs Enforcement, Office of Financial Management, Karen Eckert, Acting Director, Policy and Planning, Federal - Preparer

>>> "Eckert, Karen P" <Karen.P.Eckert@dhs.gov> 7/19/2006 11:32:45 AM >>>

I'm sorry this is late, I am forwarding the corrected comment to you.

thanks,

Karen P. Eckert
Acting Director, Policy and Planning
Office of Financial Management
8/29/2006

Comments
Federal Accounting Standards Advisory Board,
Proposed Statement of Federal Accounting Concepts Entitled
Definition and Recognition of Elements of Accrual Basis Financial Statements

Background

FASAB is requesting for comments on the exposure draft entitled "Definition and Recognition of Elements of Accrual – Basis Financial Statements." The Board is proposing to define the five elements of accrual-basis financial statements. These five elements are assets, liability, Net Position, revenue and expense. This concept would also establish two recognition criteria or conditions that must be met in order for an item is included in the financial statements. First, the item must meet the definition of an element (assets, liability, Net Position, revenue and expense) and second, the item must be measurable in monetary units. An item that meets the definition of an element but is not measurable would be a candidate for disclosure in the notes to the financial statements or as supplementary information.

The reason for this proposed change in Federal accounting standards is the result of questions that have risen about the usefulness of certain definitions of the elements in the current standards. It appears that the major issue driving this proposed concept statement is the ability of the Federal Government to change the law that will, in affect, reduce or eliminate certain type of liabilities or otherwise enable the government to avoid settlement of an obligation.

My response is as follows:

I agree with the "Proposed Concepts" as listed in the document. However, the Alternative View concerning the government's ability to change the law for nonexchanged transactions is based on the evidence of whether a present obligation exists and may preclude recognition of a liability. This approach should also be disclosed in the Notes to the Financial Statements along with the Proposed Concept is approach which cites the definition of liability must be based on existing conditions, including current law and that government has a present obligation, even if conditions change before the settlement is due. Thus, both positions should be disclosed in the Notes to the Financial Statements in order to provide the reader with full disclosure of the issue.

Comments
Federal Accounting Standards Advisory Board,
Proposed Statement of Federal Accounting Concepts Entitled
Definition and Recognition of Elements of Accrual Basis Financial Statements
Question 1.a. Should the definitions of assets and liabilities derive from they fundamental or essential characteristics?

Yes. Assets are the financial resources that are to be consumed in the entity's operation in performing its functions.

#9 – Nuclear Regulatory Commission, Carl Fredericks, Senior Systems Accountant, Federal - Preparer

>>> "Carl Fredericks" <CAF1@nrc.gov> 7/28/2006 9:08 AM >>>
Wendy,

The Nuclear Regulatory Commission has received and reviewed the FASAB Exposure Draft; "Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements and the questions on pages 4

through 9. We provided comments to Daniel Fletcher at DOI to be incorporated into the consolidated comments that will be provided by the CFO Council. We have no further comments at this time.

Thank you for the opportunity to review this FASAB Exposure Draft.

Carl Fredericks
Senior Systems Accountant
Nuclear Regulatory Commission
(301)-415-6285

**#10 – Nuclear Regulatory Commission, Office of the Inspector General,
Robert Woodward, Federal -Auditor**

>>> "Robert Woodward" <RLW3@nrc.gov> 8/2/2006 9:27:10 AM >>>
Ms. Comes,

Thank you for the opportunity to comment on the FASAB Exposure Draft titled, *Definition and Recognition of Elements of Accrual-Basis Financial Statements*.

Please find the "Questions for Respondents" section attached.

Sincerely,

Robert Woodward
U. S. Nuclear Regulatory Commission
Office of the Inspector General

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Yes. This approach is easy to understand and apply. This approach logically provides the foundation for the definitions of net position, revenues, and expenses.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Yes. No additional comments provided.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Agree, although the ability for agencies to set capitalization levels (SFFAS #6) may need to be revisited, so as to narrow capitalization ranges. Greater uniformity in this area could add value to the consolidated financial statements of the U.S. Government.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues and expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

No.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Disagree.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

The proposed Concepts Statement seems reasonable, as existing conditions

should be used to determine existing liabilities. No assurances can be made regarding the future.

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Agree. No additional comments provided.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

No.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Agree.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?

No.

6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Yes.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Yes.

7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

No.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

No comments provided.

9. The proposed Concepts Statement defines "measurable" as "means quantifiable in monetary units." (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable ("measurability probability"), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit

acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

No comments provided.

- 10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A:)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

The Alternative View could help better clarify recognition criteria. The addition of qualitative characteristics would only enhance the overall definition.

#11 – Management Concepts Inc., Chuck Maloney, Executive Director, Non-Federal - Other

August 1, 2006

Reference: Proposed SFFAC "Definition and Recognition of Elements of Accrual-Basis Financial Statements"

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6L17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

Thank you for the opportunity to respond to FASAB's exposure draft of the proposed Statement of Federal Financial Accounting Concepts "Definition and Recognition of Elements of Accrual-Basis Financial Statements." We are pleased to provide the following comments in direct response to FASAB's questions:

1.a. Should the definitions of assets and liabilities derive from their fundamental or essential characteristics?

Yes. Assets and liabilities are basic elements of financial reporting and are the components from which financial statements are developed. They must be defined as an initial portion of constructing an accounting framework. It is appropriate to define these items based on their essential elements.

1.b. Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities?

While in general it would be appropriate to define net position, revenues, and expenses based on the definitions of assets and liabilities, this method may not consider all aspects of revenues and expenses in the U.S. federal government environment, such as "financing sources" and "imputed costs."

Currently, a "financing source" can be considered to fit within the category of "revenues" as demonstrated by its display in the 5000 series of USSGL accounts, and an "imputed cost" considered an "expense" as demonstrated by its inclusion in the 6000 series. However, these items do not fit the proposed definitions, since neither results in a change of assets or liabilities when recorded by entities.

Since the element definitions must apply at entity level as well as for government wide reporting, this confusion must be considered. A possible solution is to define separately those items that are unique to federal accounting.

1.c. If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material?

Yes. The federal government environment includes items that while not measurable, are clearly assets by all other aspects. An example is natural resources. If natural resources meet the other aspects of the definition, but are not measurable, they should be considered an asset. While a commercial entity may have a reporting problem with such an item, federal financial reporting can accommodate these items as they do for stewardship assets.

2. a. Are there additional elements of accrual-based financial statements that should be defined in the Concepts Statement?

Yes. Those items that are unique to federal reporting should be defined, including "Financing Sources," "Imputed Costs," and "Long-term Commitments."

2. b. Do you agree or disagree that there are additional elements that need to be defined?

We agree. In addition to "financing sources" and "imputed costs," long term commitments of the federal government (entitlements such as social security and Medicare) should be defined and described. This would consist of the actuarially-determined amount that is expected to be ultimately paid in future years based on current laws and current participants.

3. a. Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability?

We agree with the proposed Concepts Statement. Changes to laws that affect future benefits can not and should not be anticipated in financial reporting. The present situation should be presented, that is, what the current laws provide.

4. a. Do you agree that these two characteristics are essential characteristics of all federal government assets?

Yes.

4. b. Are there additional characteristics that are fundamental or essential to all federal government assets?

No.

5. a. Do you agree or disagree that these two characteristics are essential characteristics of all federal liabilities? Please provide the reasons for your views. If you disagree give an example of an obligation or commitment that you believe is a liability but does not possess one or both of the characteristics.

We agree with the reasoning provided in the Exposure Draft.

5. b. Are there additional characteristics that are fundamental or essential to all federal government liabilities?

No.

6. a. Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived?

Yes.

6. b. Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities?

Yes.

7. a. Are there other criteria that should be established as conditions for recognition?

No.

8. a. **Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for explicit for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element?**

We agree with the proposed Concept Statement per the reasons provided in the Exposure Draft.

9. a. **Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for explicit for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item is measurable?**

We agree with the proposed Concept Statement. We do not agree with the Alternative View that explicit statements of probability.

10. a. **Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria?**

We agree with the proposed Concept Statement. We do not believe that a consideration of the qualitative characteristics of financial reporting is required in determining whether an item meets the recognition criteria.

I hope these responses are clear and helpful. We would be happy to provide any further clarification FASAB requires.

Sincerely,



Charles J. Maloney, Jr., CGFM
Executive Director
Financial Management Programs

slb

#12 – Department of Education, Gary Wood, Director of Financial Operations, Federal -Preparer



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE CHIEF FINANCIAL OFFICER

August 2, 2006

Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mail stop 6K17V
441 G Street NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

We are in receipt of your Exposure Draft of a *Proposed Statement of Federal Financial Accounting Concepts Definition and Recognition of Elements of Accrual-Basis Financial Statements*. We appreciate the opportunity to review the Exposure Draft and provide comment.

We have reviewed the Exposure Draft and found it to be informative and insightful. We understand the importance of FASAB's review and extension of its conceptual framework and the important role that the Exposure Draft plays. We take our responsibility for financial reporting seriously and have circulated the Exposure Draft internally for review and comment. We have no comment on the Exposure Draft at this time. We will continue to hold discussions with our financial reporting team and with staff from other areas of the Department of Education's financial management structure to ensure that we remain focused on the Exposure Draft and the important work ahead.

Thank you again for the opportunity to review and respond to the Exposure Draft. We look forward to seeing it in its final form.

If you have any questions, please contact me at (202) 401-0862.

Sincerely,

A handwritten signature in dark ink that reads "Gary Wood".

Gary Wood
Director, Financial Management Operations

400 MARYLAND AVE., S.W., WASHINGTON, DC 20202
www.ed.gov

Our mission is to ensure equal access to education and to promote educational excellence throughout the nation.

#13 – Department of Defense Office of the Inspector General, Carolyn Davis, Deputy Assistant Inspector General for Audit Policy and Oversight, Federal Auditor

>>> "Davis, Carolyn R., OIG DoD" <Carolyn.Davis@dodig.mil> 8/2/2006 1:47 PM >>>

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes,

We have reviewed the attached exposure draft on the proposed Statement of Federal Financial Accounting Concepts (SFFAS) on "Definition and Recognition of Elements of Accrual-Basis Financial Statements". The Defense Financial Auditing Service (DFS) within the Office of the Inspector General Department of Defense prepared the comments below in response to the specific questions contained on pages 4 – 9 of the exposure draft.

Thank you for the opportunity to provide input on this important matter. Should you have any questions, please contact Carolyn R. Davis, Deputy Assistant Inspector General for Audit Policy and Oversight, at (703) 604-8877 or by e-mail at carolyn.davis@dodig.mil.

Respectfully submitted,

Carolyn Ramona Davis, CDCMA, CDFA, CPA, MS
Deputy Assistant Inspector General for Audit Policy and Oversight
Internal Audit and Contracted Audit Services
Department of Defense Office of the Inspector General
400 Army-Navy Drive (APO-1014)
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"The true test of character is not how much we know how to do, but how we behave when we don't know what to do." John Holt

DFS Comments on the FASAB Exposure Draft: "Definition and Recognition of Elements of Accrual-Basis Financial Statements Proposed Statement of Federal Financial Accounting Concepts," June 7, 2006

1.a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your positions and any alternative approach(s) you would take to define assets and liabilities.

Yes. The definitions of assets and liabilities should derive from their fundamental or essential characteristics. Basing the definitions of assets and liabilities on their fundamental or essential characteristics provides a sound and clear foundation that can guide agencies in making decisions about classification and in understanding the basis for accounting and reporting standards that the FASAB may develop in the future.

1.b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses.

Yes. The definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities. Because the net position, revenues and expenses directly result from the actions an agency takes in regard to the assets and liabilities, it is logical that the definitions for net position, revenues and expenses would be derived from the definitions of assets and liabilities.

1.c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reason for your position

Yes. If an item meets the definition of an asset, it is an asset even if it is not recognized in the body of a financial statement because it is not measurable or its amount is not material. The first determination to be made is whether an item meets the definition of an asset (i.e., should be classified as an asset). The second determination to be made is whether the asset should be recognized on the financial statements which is a separate and distinct determination from classification. The essential characteristics of an asset, as defined in the Exposure Draft paragraphs 20 through 34, would remain with the item regardless of whether or not it is recognized on the financial statements. For example, under current accounting standards stated in SFFAS 29, "Heritage Assets and Stewardship Land," July, 2007, agencies report information on heritage assets and stewardship land in a note to the balance sheet. Although heritage assets and stewardship land are not recognized in the body of the financial statements, they are still assets. The note disclosure provides the user of the financial statements with important information that makes the financial statements useful and informative even though dollar values may not be reported for the items.

2.a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

There are no additional elements of accrual-basis financial statements that should be defined in the Concepts Statement.

2.b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

We disagree that there are additional elements that need to be defined.

3.a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement paragraph 44, that a liability must be based on "existing conditions, including current law" and that "the government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability." The determination of whether a present obligation and liability exist should be based on the known conditions, and current law in effect, at the time of the determination and not on future speculative or possible changes in law. Considering the government's ability to change the law, which is the position of the alternative view, may cause agencies to consider an additional element of uncertainty in making their determinations regarding whether a present obligation exists. The consideration of that uncertainty may cause agencies not to recognize a liability and therefore understate the government's responsibilities and decrease the reliability and usefulness of the information reported in the financial statements.

4.a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Yes. We agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government assets.

4.b) Are there any additional characteristics that are fundamental or essential to all federal government assets?

There are no additional characteristics that are fundamental or essential to all federal government assets.

5.a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Yes. We agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government liabilities.

5.b) Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

There are no additional characteristics that are fundamental or essential to all federal government liabilities.

6.a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? If not, how would you modify the definitions?

Yes. The definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

6.b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definition?

Yes, the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

7.a) Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

There are no other criteria that should be established as conditions for recognition.

8.a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

We agree with the position taken in the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element. The proposed Exposure Draft recognizes that judgment is required in making conclusions about the existence of elements (paragraph 7) and about whether items possess the essential characteristics (paragraph 60). Specifically, paragraph 7 states that "Conclusions about the existence of an element require judgment as to whether, based on the available evidence, the item possesses the essential characteristics of that element." As part of the decision-making process (i.e., judgment), an individual would use the concept of "probability" to weigh various factors, based on available evidence, in order to conclude on whether an item meets the definition of an element.

9.a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

We agree with the position taken in the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable. As part of the decision-making process (i.e., judgment), an individual would use the concept of "probability" to weigh various factors, based on available evidence, in order to conclude on whether an item is measurable.

10.a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position?

We agree with the position taken in the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Because SFFAC 1 states that the information in financial reports must have the basic characteristics of understandability, reliability, relevance, consistency, and comparability in order to effectively communicate to those who use financial information, it is reasonable that those same basic characteristics should be used in considering whether items meet the recognition criteria and should therefore be reported in the financial statements. As a result, the ED should explicitly acknowledge that the qualitative characteristics need to be considered in making decisions on whether an item meets the recognition criteria.

#14 – US Aid, Office of the Inspector General, Andrew Katsaros, Federal - Auditor

>>> "Katsaros, Andrew (IG/A/FA)" <AKatsaros@usaid.gov> 8/3/2006 11:48 AM >>>
Ms. Comes,

Attached are responses from the USAID Office of Inspector General to questions on the proposed Concept Statement on Accrual-Basis Financial Statements.

Thank you for the opportunity to comment. Please call or email if you have any questions concerning the response.

Andrew Katsaros
202-712-4902

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Yes. This is a simple approach to understanding assets and liabilities and serves its purpose in providing a basic understanding of the elements of financial statements.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Yes. This also meets the intent of providing a basic understanding of financial statement elements.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Yes. However, as indicated in the ED, many items can meet the definition of an asset, yet still not be disclosed in the notes. The reference to these items as “candidates” for disclosure should eliminate any confusion.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues* and *expenses*. (See paragraphs 2, 3, 35–37, and 56.)
- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

No.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Disagree.

3. The proposed Concepts Statement addresses the government’s ability to change laws in the future as stated in paragraph 44 as follows:
- To meet the definition of a liability, the federal government’s contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government’s power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government’s power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a

present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

I agree with the Alternative View. Through legislation, the government can affect the recognition of current liabilities and this should be recognized in the proposed Concepts Statement.

- 4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)
 - a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Agree.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?
- 5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)
 - a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Agree.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?
- 6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.
 - a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Yes.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Yes.

7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)
- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

No. Again, this definition appears sufficient for the purpose of the Concepts Statement.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page)

- b) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

I agree with the proposed Concepts Statement. It might be best to have a more complete discussion of the threshold assessment factors along with additional information on inconsistencies between reporting entities before prescribing a requirement for a probability assessment.

9. The proposed Concepts Statement defines "measurable" as "means quantifiable in monetary units." (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does

discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page)

- b) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

I agree with the proposed Concepts Statement. The rationale for measuring items can be justified in many ways. An assessment may not ultimately provide any different conclusions but instead be used to support an initial judgment.

- 10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

I agree with the Alternative View. Identifying this information in the proposed Concepts Statement would not appear confusing.

**#15 – Center for Economic and Policy Research, Dean Baker, Co-Director,
Non-Federal - Other**

Center for Economic and Policy Research
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August 3, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
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441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

I would like to comment on the proposed FASAB rules for recognizing elements of accrual basis financial statements of the federal government. The specific points I wish to raise relate to the proposed treatment of the long-term liabilities of the Social Security and Medicare programs.

I believe that the rules error in treating the long-term obligations for these programs as being current liabilities for three reasons:

- 1) There is not a legal obligation for these expenditures beyond the funding available through the trust fund;
- 2) The spending path in these projections is not plausible, at least in the case of Medicare;
- 3) Long-term spending commitments in these programs are not qualitatively different from expenditures for which projections are not made.

I will very briefly elaborate on these points.

First, in the cases of Social Security and Medicare, it is important to distinguish between the legal obligations of the programs (what would be paid under current law) and scheduled benefits which have no standing under current law. Under current law, both programs are obligated to pay scheduled benefit as long as there is money in the trust fund to pay these benefits. Under the law, these programs have no claim whatsoever on government revenue once their respective trust funds have been exhausted. While it would be politically difficult for any future Congress to cut or eliminate funding for these programs, it would be politically difficult for Congress to fail to provide a large number of government services.

FASAB does not propose including projections of future transportation or education spending its accounting of government liabilities. On what basis does it therefore include government commitments for Social Security and Medicare for which there is no current legal obligation?

The second point has to do with the plausibility of the underlying projections for Medicare. The Congressional Budget Office and the Medicare trustees make projections for Medicare assuming that there are never any major changes to the operation of the United States health care system. These projections imply that per person health care costs (adjusted for aging) will continue to vastly outpace growth in per capita income. While this may be a reasonable projection of what the world would look like if nothing changed, it is a highly improbable vision of the future.

The United States already spends more than twice as much per person as the average for other wealthy countries, all of whom enjoy longer life expectancies than the United States. The projections imply that in 30 years, the United States will spend almost 4 times as much per person on health care as other wealthy countries. It seems absurd to argue that this is a plausible state of the world. If this actually happened, it would have a devastating impact on the U.S. economy. Furthermore, it would be difficult to imagine how (or why) the United States could keep its citizens from traveling to other countries in pursuit of better and cheaper health care. It is one thing to make projections that are based on uncertain events. It is quite another to make projections based on a set of future events that is almost unimaginable. It is certainly difficult to understand what would be the meaning of liabilities of this nature.

Finally, the decision to make detailed projections for future Medicare and Social Security expenditures is a political decision. It is also a political decision to not make comparable long-term projections for other areas of spending such as corrections and defense. It would be just as easy to construct scenarios for long-term spending in these areas that would be based on projecting current trends forward. For example, if the recent trend in incarceration rates continues (a slowdown from the growth path of the eighties and nineties) the country will be spending more than 2.7 percent of GDP on corrections by 2025, with the figure rising further in subsequent years. ¹

In the same vein, China's economy is projected to be more than twice as large as the U.S. economy by 2050. If government projections assumed a need to match China's defense spending to maintain U.S. preeminence, and if China was projected to spend 3 percent of its GDP on defense, then the projections would imply that defense spending by 2050 would be more than twice as high as the projections currently in the long-term projections from the Congressional Budget Office and the Office of Management and Budget. Again, the decision not to make such detailed projections is a political decision, not one rooted in financial or accounting principles.

While these long-term projections of expenditures may involve a somewhat different commitment than the commitment to provide an income and health care for retirees (actually, the commitment to provide food, shelter, and medical care for the incarcerated is not so obviously different), these are expenditures that will confront the U.S. government in future years. It will have the option to change policies so that the expenditure path does not follow the one indicated by current projections, but it has the option to alter the spending paths for Social Security and Medicare as well.

For these reasons, it seems that the decision to treat the long-term obligations of Social Security and Medicare as current liabilities of the U.S. government is a political one. It does not have a solid foundation in economics or accounting.

Sincerely,

Dean Baker
Co-Director

¹ Most of this spending would be at the state and local levels.

#16 – NASA OIG, Mark Jenson, Acting Director - Financial Audit Statements, Federal - Auditor

>>> "Chulumovich, Madeline (HQ-WAH10)" <madeline.chulumovich@nasa.gov> 8/3/2006 5:12 PM >>>

<<NASA OIG Comments on Concepts Statement ED.doc>>

Attached are NASA OIG comments.

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**NASA OFFICE OF INSPECTOR GENERAL
COMMENTS ON EXPOSURE DRAFT
PROPOSED STATEMENT OF FEDERAL FINANCIAL ACCOUNTING CONCEPTS
“Definition and Recognition of Elements of Accrual-Basis Financial Statements”**

1. Two principles underlie the FASAB’s approach to defining and recognizing elements of accrual-basis financial statements of the federal government. The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)
 - a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.
 - b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

NASA response:

a) We agree that the definitions of assets and liabilities should derive from their fundamental or essential characteristics. Since readers will rely on the definitions in making accounting classification decisions, the definitions should include all of the essential characteristics.

b) The definitions of net position, revenues, and expenses are derived from and interrelated with the asset and liability definitions. In making judgments about the classifications of transactions, accountants will consider these relationships.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

NASA response:

c) We agree that as long as the item meets the definition of an asset and is measurable, it is an asset. If an item is measurable, then it meets the fundamental accounting principle of "units of measurement." However, materiality should not be a factor in determining whether an item is an asset, unless, materiality referred to here is used in the context of whether item should be capitalized.

* * * * *

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues, and expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

NASA response:

We believe that the five elements in the proposed Statement are adequate to define the classes of items on financial statements. We do not believe there are additional elements that need to be defined.

* * * * *

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change

a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44.

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

NASA response:

We agree with the current wording in the proposed Statement regarding the government's ability to change laws. Although the government can impact its own obligations through its power to change laws, the liabilities recognized in the financial statements must be based on present or existing conditions as of the balance sheet date. If a liability was originally recognized when previous conditions or laws were in effect, but those laws have been revised such that the liability is no longer enforceable as of the balance sheet date, the liability is no longer valid and should be written off.

* * * * *

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.
- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

NASA response:

The definition of an asset in the proposed Statement is: “An asset is a resource that embodies economic benefits or services that the federal government can control.” We propose that this definition be modified to read as follows: “An asset is a resource that

embodies probable future economic or non-economic benefits or services that the federal government can control.”

We propose this revised definition for the reasons given below.

- *Adding the word “non-economic” to describe the benefits embodied in assets*
 - *Although many federal government assets provide economic benefits which result in inflows of cash, cash equivalents, goods, or services, there are other assets which provide neither economic benefits nor “services” as defined in paragraph 25 of the proposed Statement. For example, NASA builds and launches space exploration vehicles which provide the benefit of knowledge of outer space to NASA and to the general public. The benefits provided by these assets are not necessarily economic in nature, nor do they provide a “service.” In summary, we believe that adding the word “non-economic” would broaden the nature of “benefits” embodied in assets in the context of the federal government, particularly NASA.*
- *Adding “probable future” to describe the benefits embodied in assets*
 - *If the assessment of future probability is not included in the definition, readers will have no parameters that can be used to judge whether items should be recognized as assets. Since one of the objectives of federal financial reporting is to assist report users in evaluating an agency’s financial position in the present as well as the future, it is essential that amounts recognized as assets represent items that are capable of providing benefits beyond the current reporting period and that the future benefits be considered probable.*

We do not believe there are any additional characteristics that are fundamental or essential to all federal government assets.

* * * * *

- 5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)**
- a) **Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.**
 - b) **Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?**

NASA response:

The proposed definition of a liability is: **“A liability is a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand.”** We propose that the definition be modified to read as follows: **“A liability is a present obligation of the federal government which represents the probable future outflow of assets or services to another entity.”**

- Adding “probable future outflow” to the description of assets or services provided to another entity
 - If the assessment of future probability is not included in the definition, readers will have no parameters that can be used to judge whether items should be recognized as liabilities. Since one of the objectives of federal financial reporting is to assist report users in evaluating an agency’s financial position in the present as well as the future, it is essential that amounts recognized as liabilities represent obligations that considered probable on the balance sheet date.
- Removing “at a determinable date, when a specified event occurs, or on demand.”
 - We do not agree that it is necessary for an agreement to exist between the federal government and the other entity as to timing of the settlement of an obligation in order for a liability to be recognized. For example, contingent liabilities such as estimated litigation losses or estimated environmental cleanup costs should be recognized once they are considered probable and measurable, even though the dates of future payments to reduce or eliminate the liability are unknown.

We do not believe there are any additional characteristics that are fundamental or essential to all federal government liabilities.

* * * * *

6. As indicated in Question 1a), the first principle of the Board’s approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.
 - a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?
 - b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

NASA response:

(a) See our response to Questions Number 4 and 5.

b) Revenue

*The definition of revenue in the proposed Concepts Statement is: **A revenue is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity (excluding borrowing) performed during the reporting period.***

*We propose revising the definition as follows: “**A revenue is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity relating to the entity’s ongoing programs and missions.**” This definition incorporates the concept that activities which are fundamental to an entity’s ongoing major or central operations are considered revenue. We believe that incorporating this language into the FASAB definition would benefit federal government users, because the current wording of “any other activity....performed during the reporting period” is too broad and vague.*

Expense

*The proposed definition is: **An expense is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or any other activity (excluding repayments or borrowing) performed during the reporting period.***

*We propose revising the definition as follows: **An expense is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or carrying out other activities that relate to an entity’s ongoing programs and missions during the reporting period.** This definition incorporates the concept that activities which are fundamental to an entity’s ongoing major or central operations are considered an expense. We believe that incorporating this language into the FASAB definition would benefit federal government users, because the current wording of “any other activity....performed during the reporting period” is too broad and vague.*

* * * *

7. The proposed concepts statement establishes two conditions (“recognition criteria”) that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

NASA response:

We agree with the recognition criteria in the proposed Statement.

* * * * *

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of

future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities.

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

NASA response:

We agree with the alternative view expressed in paragraphs A1 through A4 of the proposed Statement that the proposed Concepts Statement should clearly state that probability should be “assessed as part of determining whether an item meets the definition of an element (existence probability)....” Our view is that one probability standard applicable in all cases could be used.

As we stated in our response to Question #4, we propose that the word “probable” be included in the definitions of assets and liabilities. If the assessment of future probability is not included in the definitions, readers will have no parameters that can be used to judge whether an amount is an asset or liability or another element. Also, we believe that one result of adding the probability assessment to the Statement will be increased reliability and consistency in government financial statements.

* * * * *

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the

available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities.

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

NASA response:

We do not agree with the Alternative View that the Statement should be revised to explicitly state language about the application of thresholds to determine probability of measurement. We believe that readers understand the application of measurability. However, we suggest adding the following sentence to the Statement for further clarification: “An item is measurable if it can be determined with reasonable certainty or is reasonably estimable.”

* * * * *

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative

characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

NASA response:

We agree with the Alternative View that language should be added to the Statement that consideration of the qualitative characteristics should be a part of recognition decisions. Readers should be informed that the decision to recognize an item must include an assessment of such characteristics as relevance and reliability. We also believe that the proposed Statement should include a description of the qualitative characteristics. As stated in Paragraph A9, if the other conceptual framework projects do not address the characteristics, they should be addressed in this Statement.

#17 – OECD, Barry Anderson, Head, Budgeting and Public Expenditures Division, Non-federal - Other

Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory
Board
441 G Street NW, Suite 6814
Mailstop 6K17V
Washington, DC 20548
United States

3 August 2006

**Re: Exposure Draft of a Proposed Statement of Federal Financial
Accounting Concepts: Definition and Recognition of Elements of
Accrual-Basis Financial Statements**

Dear Mrs. Comes:

OECD Secretary General, Angel Gurría, asked me to respond to David Mosso's letter of June 13, 2006 that relayed the Federal Accounting Standards Advisory Board's (FASAB) request for comments on an Exposure Draft of a Proposed Statement of Federal Financial Accounting Concepts concerning the Definition and Recognition of Elements of Accrual-Basis Financial Statements.

I welcome the opportunity to comment on the proposed Exposure Draft (ED). OECD's Working Party of Senior Budget Officials (SBO)—which my unit staffs—is very concerned with the application of accounting concepts to budgets and other financial statements. In fact, the Working Party established a Network on Financial Management specifically to review government accounting frameworks and focus on the issues associated with the adoption of accrual concepts in budget statements. Meetings of the SBO Network on Financial Management have brought members and staff of international accounting standards boards (including FASAB) and budgeting officials together annually for the past 6 years. Thus, we are very cognizant of the impact accounting standards and concepts can have on budget accounting. We also recognize the leadership FASAB can have in the international accounting standards community.

Because of our long interest in federal accounting standards and concepts, we are very concerned with one of the changes to US federal financial accounting concepts proposed in the ED. Specifically, we question the reasoning behind the proposed change of the definition of a liability. The nature of the federal government is truly unique, with characteristics and powers that no other entity—individual, corporation, or sub-national government—possesses. These characteristics and powers were one of the major reasons why a separate accounting standards board was created for the US Federal Government. These characteristics and powers permit the federal government to do things that no other entity can do. Specifically, the federal government—and the federal government alone—has the power to alter unilaterally its promises in the future. Stated another way using some of the language of the ED, the federal government has the power to change unilaterally a present obligation. No other entity can do this, yet the

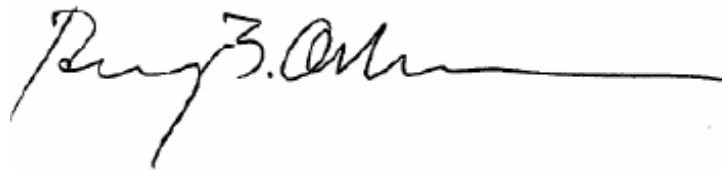
ED would use the same concept—a “liability”—to describe these transactions as are used to describe much different kinds of transactions made by other entities that do not have the powers of the federal government.

My point here is not to say that these transactions don’t belong somewhere in the federal government’s financial statements. It is only to say that classifying these transactions the same as private sector liabilities is **wrong**: they are different and deserve a special classification—perhaps as “social obligations” or some other name, and perhaps as supplemental information to the financial statements, but not as “liabilities”. The Executive Summary of the ED states that the Board “anticipates that the guidance in the Concepts Statement would enhance the understandability, consistency, and comparability of financial reporting”. We suggest that implementation of this new concept as stated in the ED would do exactly the opposite: confuse users of financial statements by leading them to believe that the liabilities reported for certain federal transactions have the same status as liabilities reported for private entities.

Other OECD countries have also wrestled with the issue of how to classify transactions that are unique to the federal government, but we are not aware of any that have decided to lump the federal government’s “social obligations” in the same category as private liabilities. In fact, all federal governments that we are aware of have *explicitly* decided not to call federal “social obligations” liabilities. However, we know that this issue continues to be very important to all OECD member countries. Thus, we will add this issue to the agenda of our 2007 meeting of the SBO Network on Financial Management, which is tentatively scheduled for March 5-6 in Paris. Whatever the outcome of your deliberations, representatives from FASAB will be invited to present their views, as will representatives from international accounting standards boards and from other OECD member countries and their accounting standards boards. I suggest that you may want to consider the outcome of this meeting before adopting a new Statement of Federal Financial Accounting Concepts.

I would be happy to discuss this issue further with you or any of the Board members, and I look forward to seeing you and/or any members of FASAB at the meeting of the SBO Network on Financial Management in Paris next year.

With best regards,

A handwritten signature in black ink, appearing to read "Barry Anderson", with a long horizontal line extending to the right.

Barry Anderson
Head, Budgeting and Public

Expenditures Division

#18 – Veterans Affairs, Robert J. Henke, Assistant Secretary for Management, Federal-Preparer



DEPARTMENT OF VETERANS AFFAIRS
ASSISTANT SECRETARY FOR MANAGEMENT
WASHINGTON DC 20420

AUG - 3 2006

Ms. Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mail stop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

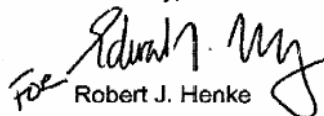
The Department of Veterans Affairs (VA) appreciates having an opportunity to comment on FASAB's exposure draft of a proposed Statement of Federal Financial Accounting Concepts entitled *Definition and Recognition of Elements of Accrual-Basis Financial Statements*.

VA does not support FASAB's position contained in the exposure draft because the definition of a liability would most likely require that future-scheduled social insurance obligations be reported as liabilities on both agency and governmentwide financial statements.

VA does not believe that future-scheduled social insurance obligations are liabilities because they are neither contractual commitments nor present obligations of the Federal government. In addition, benefits for individuals are not directly tied to taxes they have paid, meaning that benefit entitlements are not exchange transactions. Further, VA does not consider future-scheduled social insurance obligations as measurable from an audit perspective.

For the reasons outlined above and in the responses to the "Questions for Respondents" document enclosed, VA does not concur with the FASAB exposure draft. Please contact me at (202) 273-5588, or Edward Murray, Deputy Assistant Secretary for Finance, at (202) 273-5504 with any comments or questions.

Sincerely,


for Robert J. Henke

Enclosure

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

Question 1(a):

Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Response 1(a):

Yes, the definitions of assets and liabilities should derive from their fundamental or essential characteristics. This gives more specificity in helping agencies identify assets and liabilities.

Question 1(b):

Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses.

Response 1(b):

Yes, the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. These definitions are logical from an accounting standpoint and provide clarity to agencies.

Question 1(c):

If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reason for your position.

Response 1(c):

Yes, if an item meets the definition of an asset it should be considered an asset even though it would not be recognized on the financial statements. The proposed Concepts Statement states that "An asset that is not recognized in the body of the financial statements would be a CANDIDATE for disclosure in the notes."

Currently, agencies are required to reference a note on the balance sheet that discloses information about heritage assets and stewardship land, but no asset dollar amount should be shown. The note disclosure provides minimum reporting requirements, including a description of major categories, physical unit information for the end of the reporting period, physical units added and

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

withdrawn during the year, a description of the methods of acquisition and withdrawal, and condition information.

In addition, an item can also be an asset and not disclosed in the financial statement footnotes, if it can't be measured or is not material. Doing so would be excessive to preparers of financial statements and would result in less relevant information for readers of the financial statements. Therefore, VA agrees that definition and recognition are separate concepts.

Question 2(a):

Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Response 2(a):

Recognizing that FASAB has a project related to social insurance and the applicability of liability definitions, there should be an expectation that additional elements may be contained there. Perhaps this Concepts Statement should refer to these other projects.

Question 2(b):

Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Response 2(b):

Although most items can be categorized as an asset or a liability, the nature of some items do not fit the stringent definitions of either. For example, social insurance obligations are somewhat different than traditional liabilities. Future scheduled social insurance benefits are not present obligations of the Federal government nor are they contractual commitments of the Federal government. In addition, benefits for individuals are not directly tied to taxes they have paid, meaning that benefit entitlements are non-exchange transactions. VA believes that FASAB should consider an additional element to better define social insurance obligations as future scheduled benefits and that they should not be considered liabilities.

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

Question 3(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Response 3(a):

Due to the fact that the Federal government has the right to alter scheduled benefits in any manner at any time, VA supports the alternative view that the government's power to change laws affects the existence of a present obligation.

Question 4(a):

Do you agree that these two characteristics are essential characteristics of all Federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Response 4(a):

Yes, VA agrees that there are two characteristics that are essential characteristics of all Federal government assets: (1) it is a resource that embodies economic benefits or services; and (2) the Federal government can control it.

Question 4(b):

Are there any additional characteristics that are fundamental or essential to all Federal government assets?

Response 4(b):

No, there are no additional characteristics that are fundamental or essential to all Federal government assets.

Question 5(a):

Do you agree or disagree that these two characteristics are essential characteristics of all Federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

Response 5(a):

Yes, VA agrees that there are two characteristics that are essential characteristics of all Federal government liabilities. First, it constitutes a present obligation to provide assets or services to another entity. Second, the Federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur.

Question 5(b):

Are there any additional characteristics that are fundamental or essential to all Federal government liabilities?

Response 5(b):

No, there are no additional characteristics that are fundamental or essential to all Federal government liabilities.

Question 6(a):

Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? If not, how would you modify the definitions?

Response 6(a):

Yes, the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

Question 6(b):

Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definitions?

Response 6(b):

Yes, the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

Question 7(a):

Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

Response 7(a):

No, there are no other criteria that should be established as conditions for recognition.

Question 8(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

Response 8(a):

VA concurs with the Alternative View that there needs to be an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element. Some items are improbable and should not be required to be disclosed in the body of the financial statements or the footnotes.

Question 9(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

Response 9(a):

VA concurs with the Alternative View concerning the need for an explicit requirement for an assessment of probability threshold when determining whether an item is measurable. If the item does not meet the probability threshold, it is irrelevant whether it is measurable.

Question 10(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position?

Response 10(a):

VA concurs with the Alternative View concerning the need for consideration of the qualitative characteristics of financial statements as part of determining

VA'S RESPONSES TO FASAB'S "QUESTIONS FOR RESPONDENTS"

whether an item meets the recognition criteria. For example, if there is not a specific requirement for an existence and measurability threshold, the addition of more items could cause confusion.

6/22/2006

6

8/29/2006

54 of 225

#19 – National Science Foundation, Division of Financial Management, John Lynskey, Deputy Director, Federal -Preparer

>>> "Lynskey, John H." <jlynskey@nsf.gov> 8/4/2006 11:02 AM >>>

Hi Wendy and Julia,

NSF concurs with the CFOC concerns raised on the FASAB Exposure Draft, 'Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements' that is being sent to FASAB.

In relation to the "Questions for Respondents", NSF wanted to highlight two responses that will be presented by CFOC Standardization committee to FASAB(draft attached) and provide additional comments on the liability element because it is related to the recent Liability Classification Survey that is being conducted by FASAB. These new definitions on the ED have far reaching impact on our agency, so we hope that our input will be taken into consideration.

Response 4(a) - We agree with the response. It is very important that the federal government can control the asset. An agency may have title to an asset but not control it and if that is the case, the asset should not be recognized on the entity's balance sheet.

In the ED, proposed concept under paragraph 30 should be removed as it is confusing.

Response 5(b) - In addition to the two characteristics listed, there is a third underlying characteristic in that "Governments agreement to provide assets or services to another entity must be based on existing conditions including current law". This is discussed in the ED, under proposed concept paragraph 44. This concept results in the idea of a present obligation and should be elevated to a characteristic.

While we recognize the intent of the proposed concept paragraph 36 for all federal government liabilities, we feel this definition actually increases the grayness of the definition rather than providing clarity to it since the paragraph will only increase the level of debate more than it is currently between legal liability versus accounting liability. Therefore, we feel that the proposed concept under paragraph 36 should be removed.

Additionally, to tie the definition of the liability element to the recent FASAB's project on Liability Classification Survey, we would like to highlight the proposed enhancements to the definition of non-government-related events. This new definition narrows NSF flexibility for accounting treatment to acknowledge an event even though it is the direct result of federal operations.

We are always happy to discuss these concerns with you as you gather input.

John

John Lynskey
Deputy Director,
Division of Financial Management
National Science Foundation
4201 Wilson Boulevard, rm 605
Arlington, Va 22230
703 292-4457
703 292-9005(fax)

From: CFO COUNCIL [mailto:CFO-COUNCIL@LISTSERV.GSA.GOV] **On Behalf Of** David Horn

Sent: Thursday, August 03, 2006 12:59 PM

To: CFO-COUNCIL@LISTSERV.GSA.GOV

Subject: [CFO-COUNCIL] CFOC Elements Exposure Draft Concurrence (Virus checked)

This message is being sent on behalf of Daniel Fletcher, Deputy Chief Financial Officer, Department of the Interior.

At the most recent Chief financial Officers Council (CFOC) meeting I presented the issues and concerns of the Standardization Committee related to FASAB's Exposure Draft titled, "Definition and Recognition of Elements of Accrual-Basis Financial Statements." In this presentation I discussed the alternative view presented in this draft and the importance of the CFOC supporting this view with one voice. We have modified our approach and our method of expressing this voice as follows:

- □ □ □ □ We have drafted a modified letter (please see the attached file) expressing the concerns and recommendation we would like you to support by signature on a faxed copy to be sent to you this afternoon. Please return your signed document by fax to my office at 202-208-6940 by COB today, August 3, 2006.
- □ □ □ □ We removed the attachment related to "Questions to Respondents" and will forward that to FASAB by separate cover from the Standardization Committee Chair. We encourage any agency that wishes to voice individual opinion related to these questions to do so.
- □ □ □ □ We have scheduled a teleconference for 9:00 am on Friday, August 4, 2006, for discussion with any member not comfortable supporting this position or who would like any further discussion before concurring. The call-in number is 1-866-901-9023, passcode 7503516.

We appreciate the patience and effort of all members in this initial undertaking and look forward to serving the council in the future. If you have any individual concerns that need my personal attention do not hesitate to contact me at 202-208-5225.

David C. Horn CPA, CGFM
Department of the Interior
Office of Financial Management
202-208-5542

Wendy M. Comes, Executive Director

Federal Accounting Standards Advisory Board

DRAFT CFOC LETTER AND RESPONSES REFERRED TO BY THE NSF
RESPONDENT

Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

We appreciate the opportunity to review and comment on the FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006 and offer consolidated comments from the Chief Financial Officers Council.

Initially, we would like to express our support of the concerns raised in the alternative view and look to have these concerns addressed prior to publication of the Statement of Concepts. The departure from existing definitions for assets and liabilities is significant and would require many additional items to be recognized. The addition of these items would cause the financial statements to become cumbersome to the readers and preparers and result in inconsistent treatment across accounting periods. Other standard setting bodies (FASB, GASB) have made concerted efforts not to redefine or upset current practices.

We have attached the answers to the "Questions for Respondents" to this document for your review. We look forward to working with you and your staff in the future development of this statement and other standards as they become active projects.

Sincerely,

Question 1(a):

Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Response 1(a):

Yes, the definitions of assets and liabilities should derive from their fundamental or essential characteristics. This gives more specificity in helping agencies identify assets and liabilities.

Question 1(b):

Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses.

Response 1(b):

Yes, the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. These definitions are logical from an accounting standpoint and provide clarity to agencies.

Question 1 (c):

If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reason for your position.

Response 1(c):

Yes, if an item meets the definition of an asset it should be considered an asset even though it would not be recognized on the financial statements. The proposed Concepts Statement states that "An asset that is not recognized in the body of the financial statements would be a CANDIDATE for disclosure in the notes".

Currently, agencies are required to reference a note on the balance sheet that discloses information about heritage assets and stewardship land, but no asset dollar amount should be shown. The note disclosure provides minimum reporting requirements, including a description of major categories, physical unit information for the end of the reporting period, physical units added and withdrawn during the year, a description of the methods of acquisition and withdrawal, and condition information.

In addition, an item can also be an asset and not disclosed in the financial statement footnotes, if it can't be measured or is not material. Doing so would be excessive to preparers of financial statements and would result in less relevant information for readers of the financial statements. Therefore the CFO Council agrees that definition and recognition are separate concepts.

Question 2(a):

Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Response 2(a):

Recognizing that FASAB has a project related to social insurance and the applicability of liability definitions, there should be an expectation that additional elements may be contained there. Perhaps this Concepts Statement should refer to these other projects.

Question 2(b):

Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Response 2(b):

Although most items can be categorized as an asset or a liability, the nature of some items do not fit the stringent definitions of either. The nature of social insurance obligations are somewhat different than a traditional liability. Future scheduled social insurance benefits are not present obligations of the federal government nor are they contractual commitments of the federal government and benefits do not represent exchange transactions; benefits for individuals are not directly tied to taxes they have paid, meaning that benefit entitlements are non-exchange transactions. We believe that the FASAB should consider an additional element to better define social insurance obligations as future scheduled benefits and that they should not be considered liabilities.

Question 3(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Response 3(a):

Due to the fact that the federal government has the right to alter scheduled benefits in any manner at any time, the CFO Council supports the alternative view that the government's power to change laws affects the existence of a present obligation.

Question 4(a):

Do you agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Response 4(a):

Yes, we agree that there are two characteristics that are essential characteristics of all federal government assets; (1) it is a resource that embodies economic benefits or services; and (2) the federal government can control it.

Question 4(b):

Are there any additional characteristics that are fundamental or essential to all federal government assets?

Response 4(b):

No, there are no additional characteristics that are fundamental or essential to all federal government assets.

Question 5(a):

Do you agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Response 5(a):

Yes, we agree that there are two characteristics that are essential characteristics of all federal government liabilities: (1) it is a present obligation of the federal government to provide assets or services to another entity at a determinable date (2) when a specified event occurs or on demand.

Question 5(b):

Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

Response 5(b):

No, there are no additional characteristics that are fundamental or essential to all federal government liabilities.

Question 6(a):

Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? If not, how would you modify the definitions?

Response to 6(a):

Yes, the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

Question 6(b):

Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definitions?

Response 6 (b):

Yes, the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

Question 7(a):

Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

Response 7(a):

No, there are no other criteria that should be established as conditions for recognition.

Question 8(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

Response to 8(a):

We concur with the Alternative View that there needs to be an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element. Some items are improbable and

should not be required to be disclosed in the body of the financial statements or the footnotes.

Question 9 (a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

Response to 9(a):

We concur with the Alternative View concerning the need for an explicit requirement for an assessment of probability threshold when determining whether an item is measurable. If the item does not meet the probability threshold, it is irrelevant whether it is measurable.

Question 10 (a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position?

Response 10(a):

We concur with the Alternative View concerning the need for consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. For example, if there is not a specific requirement for an existence and measurability threshold, many more items, will be recognized on the financial statements causing confusion and muddying the statements.

#20 – Social Security Administration, Dale Sopper, CFO Federal-Preparer

Rec'd 8/4/2006

FASAB - Concept Statement Exposure Draft

Definition and Recognition of Elements of Accrual-Basis Financial Statement

Page 5 -Questions for Respondents

1(a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics?

Yes. Defining assets and liabilities by their fundamental characteristics is a sound approach and will assist entities in identifying these elements.

1(b) Should the definitions of net position, revenues and expenses derive from the definitions of assets and liabilities?

Yes. Defining net position, revenues and expenses from the definitions of assets and liabilities is a logical approach and these definitions underlie those of assets and liabilities.

1(c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide a response.

Yes, an item can meet the definition of an asset if it meets the definition of an asset even if not ultimately recorded in the books of the entity as such. In order for an asset to be recognized in the financial statements it must meet the definition and recognition criteria. For example, equipment, furniture and fixtures are all in the asset element group - i.e. economic resources of the entity but because of accounting constraints (conservatism, materiality, cost vs. benefit rule, and specialized practices) which are typically part of this conceptual framework, such assets may be expensed off due to the capitalization policies and procedures of the entity. The items are first classified as assets in the property plant and equipment but due to other prevalent accounting practices are not ultimately recorded or recognized as assets on the books.

2(a) The proposed concepts Statement defines five elements of accrual-basis financial statements: assets, liabilities, net position, revenues, and expenses are there additional elements that are unique to the Federal government?

No, the elements described cover the elements used in SSA's financial statements.

2(b) Do you agree or disagree that there are additional elements that need to be defined? If so, what are the essential characteristics of these elements?

SSA does not believe additional elements need to be defined.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

SSA fully supports the alternative view. We believe that the government's power to modify existing laws affects the existence of a present obligation due to the fact that the government holds the right to change future benefits at any time.

Additionally, it should be noted that accounting and legal items typically are not used interchangeably to record accounting transactions and events. For instance, items such as intangibles have a legal life and a separate but distinct generally accepted accounting life. Intangible items are not recorded on the books based on the legal life (i.e. patent - legal life is 20 years; trademarks- automatically renew every 10 years; copyright -life of creator plus 70) but instead follow the accounting premise of indefinite or definite life and impairment accounting. Following through on that same line of

thought, subsequent events and contingent liabilities arising from legal suits are not automatically recorded as liabilities but instead for accounting purposes go through a thorough analysis phase prior to liability determination.

The above examples clearly exemplify the distinction between legal and accounting practices and treatment. Typically, the two are not intermixed on financial statements. This conceptual statement appears to be drafting accounting standards based on legal issues that could change at a drop of a hat and that truly are not measurable for the outgoing years under consideration.

4(a) Do you agree that (a) an asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits ore services, can obtain them and deny or regulate the access of other entities, are the two essential characteristics of all federal government assets?

Yes, we agree with the two proposed characteristics of federal government assets.

4(b) Are there any additional characteristics that are fundamental or essential to all federal government assets?

No.

5(a) Do you agree or disagree that (a) a liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur, are the two characteristics essential of all federal government liabilities?

Yes, we agree with the two proposed characteristics of federal government liabilities.

5(b) Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

No.

6(a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived?

Yes, we believe the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

6(b) Do the definitions of net position, revenues and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definitions?

Yes, we believe the definitions of net position, revenues and expenses adequately convey their relationship to assets and liabilities.

7(a) Are there other criteria that should be established as conditions for recognition? If so, what would you add or delete?

No.

8(a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain.

SSA agrees with the alternative view. We believe that an explicit requirement for an assessment probability threshold should be included in the discussion. This would help agencies determine whether an item meets the definition of an element. The lack of a probability threshold could open the door for many items to be unnecessarily accounted and the result would make the financial statements less meaningful.

9. a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable.

The alternative view (2) is the view of choice. The broad definition of “measurable” in view (1) raises concern that the definition is so expansive that anything could be deemed “measurable” when in fact it may not be relevant, reliable or measurable in the accounting sense of the word.

10. a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria?

The alternative view (2) is the view of choice. The qualitative characteristics should be grouped with the elements so that a comprehensive and cohesive picture is presented of the relevant factors required to make a sound accounting decision. SFFAC #1 details a general discussion on the federal reporting environment and not the specifics of providing a framework to support standardized accounting practices and decision making. The elements, qualitative characteristics and the accounting constraints (materiality, conservatism, specialized practices, and cost vs. benefit) serve as building

blocks or a step by step process to support accounting practices utilized and should be consolidated and reported within one conceptual statement.

#21 – Government Accountability Office, Jeff Steinhoff, Managing Director, Federal - Auditor



United States Government Accountability Office
Washington, DC 20548

August 4, 2006

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board

Dear Ms. Comes:

We appreciate the opportunity to respond to the Federal Accounting Standards Advisory Board's (FASAB) exposure draft (ED) on its proposed concepts statement entitled *Definition and Recognition of Elements of Accrual-Basis Financial Statements*. The GAO supports the efforts of the Board in developing conceptual accounting and reporting guidance on which federal financial accounting and reporting standards will be based.

We generally agree with the proposed concepts statement. At the same time, as discussed below, we strongly support the alternative views expressed by Bob Dacey, GAO's Chief Accountant, and other members of the Board. We hope the Board will reconsider issuing the ED as final until its efforts underway with the projects on social insurance and the liability definition are completed, as the ED's current position may require revision as a result of finalizing these projects.

We agree with the members supporting the alternative view that recognition criteria in the final statement should be comprehensive and should include all factors relevant to determining whether an item should be recognized. Providing complete criteria will prove most useful to the Board as it deliberates standards and to users as they seek to apply them. Also, we agree with the alternative view that the final statement should explicitly acknowledge that all of the qualitative characteristics of financial reporting should be considered as part of determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. The ED states that determining whether an item is measurable only means that it is quantifiable in monetary units and does not explicitly discuss consideration of whether the resulting quantification, although measurable would, for example, be relevant or reliable.

We also agree with the alternative view that the concepts statement should explicitly state what it implicitly requires. More specifically, the concepts statement should explicitly state that: (1) the probability that an item meets the definition and essential characteristics of an element should be assessed as part of determining whether an item meets the definition of an element (existence probability), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element and, thus, the item should not be recognized. Similarly, as discussed in

the alternative view, the final concepts statement should explicitly state that in determining whether an item which meets the definition of an element should be recognized (1) an assessment is required of the probability that an item is measurable and (2) there exists a probability threshold below which an item would not be deemed measurable and, thus, the item should not be recognized.

Explicitly requiring an assessment of probability in determining existence and measurability and an acknowledgement that a probability threshold exists for both would increase the consistency of implementation of the final concepts statement and in specific standards. As discussed in the alternative view, excluding such explicit requirements in the final concepts statement is more likely to result in failure to consider such probabilities, leading to many more items being recognized in the financial statements. We agree with the alternative view that the resulting financial statements would fall short in fulfilling a number of the qualitative characteristics of financial reporting, as described in the alternative view. Earlier this year, in commenting on an Invitation to Comment issued by the Financial Accounting Standards Board (FASB), we expressed serious concerns about proposed changes that would remove probability from the recognition criteria for liabilities, resulting in the recognition of liabilities that, under current standards, would be considered reasonably possible or remote and therefore would not be recognized. We questioned the value of recognizing liabilities arising from events that are unlikely to occur which, as noted above, would be a more likely outcome in federal financial statements if probability is excluded from the proposed concepts statement. If, in fact, the events did not occur, the overstated liabilities would be later reduced and income recognized by the entity.

Further, the final standard should eliminate most of the references to the term "measurement" as it is not part of the recognition criteria and is confusing. In most instances, such references should be replaced with references to measurability. Enclosed are suggested language edits to implement this comment.

Finally, as pointed out in the second alternative view, the federal government's power to modify laws that could change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. The government's ability to change laws may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability.

We appreciate the opportunity to provide our comments on the exposure draft and to express our strong support for the alternative views and would be pleased to further discuss our comments with you at a convenient time. If we can be of further assistance, please call me at (202) 512-2600.

Sincerely yours,



Jeffrey C. Steinhoff
Managing Director
Financial Management and Assurance

Enclosure

ENCLOSURE

Suggested Language Changes to Modify References to Measurement

7. The existence and measurability ~~or amount~~ (or both) of many assets, liabilities, and other elements may not be certain, but the definitions and recognition criteria in this Statement do not require certainty. Conclusions about the existence of an element require judgment as to whether, based on the available evidence, the item meets the definition of that element, which includes a consideration of whether it possesses the essential characteristics of that element. ~~Similarly, conclusions about the measurability of an element require judgment as to whether, based on available evidence, the item is measurable.~~ The measurement of an element being considered for recognition in the financial statements often will require estimates and approximations. Measurement also may require a more rigorous assessment of the probability of future inflows or outflows of resources to enhance the reliability of amounts recognized in the financial statements.
57. Uncertainty about economic activities and results is pervasive and often clouds whether a particular item qualifies as an asset or a liability at the time the definitions are applied. Whether a resource embodies economic benefits or services to which the government can control access, or whether the government has a present obligation to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand, often can be determined reliably only with hindsight. As a result, the government may have recognized as expenses or revenues some items that with hindsight actually met the definitions of assets or liabilities or vice versa. Alternatively, some items may not have been recognized because of uncertainty about whether they qualified as assets or liabilities or because of measurement measurability issues stemming from uncertainty at the time of assessment.
58. Uncertainty increases the costs of financial reporting, particularly the costs of measurement and recognition. Some items that meet the definitions of assets or liabilities may be recognized ~~as expenses or revenues~~ or remain unrecognized because a cost-benefit analysis indicates that their recognition is not useful enough to justify the necessary time and effort. It may be possible to make the information more reliable in the face of uncertainty by exerting greater effort or spending more money, but it also may not be worth the added cost.
59. A highly significant practical consequence of the features described in the preceding two paragraphs is that the existence or ~~amount~~ measurability (or both) of many assets and liabilities may not be certain. However, as discussed in paragraph 7, the definitions and recognition criteria in this Statement do not require certainty that items meet the definition of an element, which includes a consideration of whether it possesses the related essential characteristics, or that items are measurable. ~~possess the essential characteristics of particular elements in order for the items to qualify for recognition. Moreover, their measurement often will require estimates and approximations or more rigorous assessments of probability unless financial statements are to be restricted to reporting only cash transactions.~~

60. Degrees of uncertainty or probability are not part of the definitions of elements. Uncertainty about the existence of an element means that the application of the relevant definition often requires judgment about whether items possess the essential characteristics. Items that are judged to meet the definition of an element qualify for recognition if they are measurable in monetary units. Otherwise they may be disclosed. Assessments of the probabilities of inflows or outflows of economic benefits or services as a result of the existence of an element may be necessary for reliable measurement of the amount to be recognized and, if so, are part of a decision whether to recognize or disclose the element.
61. A practical result of the distinction between deciding whether an item meets the definition of an element and deciding whether an element should be recognized is that measurability (the second recognition criterion) is a more stringent hurdle for recognizing an item in the financial statements than is meeting the definition of an element (the first criterion). Based on the available evidence, the government may conclude that an item meets the definition of an element of accrual-basis financial statements. However, application of the ~~measurement~~ measurability criterion, including when appropriate an assessment of the probability of future resource flows, may result in an amount that is not material to the financial statements. If so, the asset or liability need not be recognized; ~~but it may be disclosed, together with the reasons for not recognizing it.~~ Measurability considerations also may result in postponing recognition of some assets or liabilities until their future outcomes become less uncertain or their measures become more reliable.

#22 – Institute for Truth in Accounting, Sheila Weinberg, CEO, Non-federal - Other

**Institute
for Truth in Accounting**

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August 5, 2006

(847) 835-5200 – (847) 835-3470

Wendolyn Comes, Executive Director
Federal Advisory Standards Board
441 G Street NW, Suite 6814
Mailstop 6K17V
Washington, DC 20548

Dear Ms. Comes:

Subject: Response to Exposure Draft issued June 7, 2006
Definition and recognition of Elements of Accrual-Basis Financial Statements

The Institute for Truth in Accounting (IFTA) thanks the Federal Accounting Standards Advisory Board (FASAB) for the opportunity to respond this exposure draft. The Institute, founded in 2002, is a nonprofit organization with no political affiliations. It is made up of business, academic, governmental and other leaders who are committed to high standards of ethics and integrity, and who support these principles in the private as well as in the public sector. Our mission is to enhance the credibility of public and private sector financial reporting by encouraging the issuance of understandable, reliable and relevant information.

Overall Response

IFTA commends FASAB's efforts to improve public accountability and enhance the credibility of Federal government financial reporting. Providing clearer and simpler accounting definitions is evidence of these efforts.

For this reason, IFTA supports the FASAB majority position on this proposed statement. We agree with the definitions of asset, liability, net position, revenue and expense. We would, however, express the following understanding regarding some of these definitions:

- that the use of the term present obligation in defining liabilities also encompasses the present value of obligations;
- that the return of revenue to an originating source, which decreases assets and/or increases liabilities, does not define such refund as an expense;

- that the recapture of expense due to unsatisfactory services rendered or a return of goods purchased, which increases assets and/or decreases liabilities, does not define such refund as revenue.

IFTA concurs with the recognition criteria outlined in paragraph 5 (a) and (b) of this exposure draft.

IFTA believes that it should be clearly stated within Paragraphs 5 thru 9 that “diligent effort should be taken to recognize all material elements or items, despite measurement difficulties.” The vast majority of material elements or items are measurable in a way that is superior to not measuring them at all.

Specific Response to FASAB Questions

1. Defining and recognizing elements.

- a) The definitions of assets and liabilities should be derived from their fundamental or essential characteristics. We see no alternative approach. Including verbiage not fundamental or essential to an element's characteristics would provide opportunity for directing elements away from being reported in the basic financial statements.
- b) The definitions of net position, revenues, and expenses should be derived from the definitions of assets and liabilities with the exception of refunds mentioned earlier in this response. We see no alternative approach. Net assets are simply the mathematical net of assets and liabilities. Revenue and expense give rise to assets and liabilities.
- c) An item that meets the definition of an asset **or a liability** must meet the recognition criteria to be reported in the body of a financial statement. If, **after diligent effort**, an asset **or a liability** cannot be **reasonably** measured or **reasonably** estimated **then** there is no basis for recording. In such circumstances, if the uncertainty of a recognizable item is material, such issue should be fully disclosed in the footnotes to the basic financial statements. It would be the responsibility of the financial report's auditors to issue an adverse opinion or disclaimer opinion, if a material item was not recorded in the basic financial statements, because of its inability to be reasonably measured or estimated.

2. Additional elements.

- a) To avoid certain eliminations in consolidating financial statements, it may be beneficial to define a “transfer” element. The transfer element would be defined as increases and/or decreases in assets and/or liabilities exchanged between component units of the federal government.

- b) If certain intangible resources, long-term social obligations, and other commitments meet both the elemental and recognition criteria, they should be handled according. No further additional elements need to be defined.

3. Government's ability to change laws.

Paragraph 33 of the exposure draft states, "Implicit in the definition and essential characteristics of assets is that the event giving rise to the government's ability to control access to the economic benefits or services embodied in a resource must have occurred. The government's intent or ability to acquire a resource in the future does not create an asset. For the resource to qualify as an asset, the government already must have acquired the resource or otherwise obtained access to the resulting benefits or services to the exclusion of other entities, for example, the mere existence of the government's power to tax is not an asset because, until the government has exercised that power by imposing a tax and has access to benefits by virtue of completion of a taxable event, no event has occurred to generate resources and there are no resulting economic benefits that the government can control and use in providing programs and services."

This should apply to government obligations as well. For the obligation to no longer qualify as a liability, the government must already have abandoned the obligation or otherwise revoked access to the promised benefits or services to the entitlees, for example, the mere existence of the government's power to cancel an obligation does not cancel a liability because, until the government has exercised that power by canceling a benefit and has denied access to benefits by virtue of completion of the canceling event, no event has occurred to reduce obligations and there are no resulting economic benefits that the government can control and use in providing programs and services.

The FASAB should not attempt to anticipate the action or intent of future governing bodies by assuming a future governing body will change laws. A seated governing body should not be able to hide its accountability for establishing or increasing obligations because a future governing body may change the laws that established or increased the obligations. Conversely, the public should be informed if a seated governing body reduces or eliminates existing obligations by changing current laws. Governing bodies have the ability to include provisions in current law that would increase, eliminate or reduce benefits or services in the future. Therefore if it was the intent of past and current representatives of the citizenry to increase, eliminate or reduce promised benefits or services in the future, then there would be such provisions in current law.

4. Characteristics that are *fundamental* or *essential* to *all* federal government assets.

- a) IFTA agrees that there are two characteristics essential to all federal government assets: (1) an asset embodies economic benefits or services that can be used in the future and (2) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities.
 - b) There are no *additional* characteristics that are *fundamental* or *essential* to all federal government assets.
5. Characteristics that are *fundamental* or *essential* to all federal government liabilities.
- a) IFTA agrees that there are two characteristics essential to all federal government liabilities: (1) a liability is a present obligation to provide assets or services to another entity and (2) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. A government liability is created when a law is enacted that obligates the government to provide assets or services in the future.
 - b) There are no *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities.
6. Board's approach to defining elements as deriving from their essential characteristics.
- a) The definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.
 - b) The definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.
7. Conditions that should be met for an item to be recognized in the body of a financial statement:
- There are no criteria that should be established as conditions for recognition other than (1) the item must meet the definition of an element and (2) the item must be measurable.
8. Specifically requiring or excluding an assessment of probability when deciding whether an item meets the definition of an element.

IFTA believes that probability is always an issue that must be trusted to conservative professional judgment: anticipate no gains; allow for all losses. Such judgment, which is reviewed by the financial report's auditors, is expected in the normal course of the application of the science of accounting. The specific mentioning of probability in this Concept Statement seems directed toward keeping elements off of the basic financial statements.

9. Explicitly discussing the assessment of probability that an item is measurable.

Again, IFTA believes that probability is always an issue that must be trusted to conservative professional judgment as stated above. Once again, the specific mentioning of probability in this Concept Statement seems directed toward keeping elements off of the basic financial statements. Further, if the probability of being unable to measure a recognizable element is grossly material, conservative professional judgment will require the financial report's auditors to consider an adverse opinion or disclaimer of opinion.

10. Including the qualitative characteristics of SFFAC 1 in this Statement.

If already published and not changed by this Concepts Statement, including the qualitative characteristics is unnecessary and confusing. The Concept Statement, to be effective, should limit itself to the specific subject of the concept. Including it in the Concept Statement would serve the same purpose as the specific inclusion of probability.

Members of the Institute for Truth in Accounting look forward to testifying at FASAB's hearing on September 27 or 28, 2006. Thank you again for the opportunity to comment this exposure draft. Please do not hesitate to contact us, if you have any comments or questions.

Sincerely,

Sheila A. Weinberg

Institute for Truth in Accounting
Founder & CEO

***#23 – Department of Commerce, Lisa Casias, Deputy CFO, Federal -
Preparer***



UNITED STATES DEPARTMENT OF COMMERCE
Chief Financial Officer
Assistant Secretary for Administration
Washington, D.C. 20230

AUG - 4 2006

Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

Enclosed are the Department's detailed comments to the Exposure Draft. We have significant concerns about one aspect of the proposed Concept Statement. In our response, we communicate our significant concerns about the proposed Concept Statements' dramatic expansion of the definition of a liability.

We strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, we support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

We also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, we suggest maintaining the current asset and liability definitions and including them in the proposed Concepts Statement.

We look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

A handwritten signature in cursive script, appearing to read "L. Casias".

Lisa Casias
Deputy Chief Financial Officer and
Director for Financial Management

Enclosure

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

Prepared by: Department of Commerce, Office of Financial Management

Date Prepared: August 4, 2006

Questions for Respondents

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

DOC response to 1 (a):

Yes, the Department of Commerce (DOC) agrees that the definitions of assets and liabilities should derive from their fundamental or essential characteristics.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

DOC response to 1 (b):

Net Position: The proposed definition (i.e., difference between total assets and total liabilities) is acceptable. DOC believes, however, that the definition should be expanded as stated in our answer to question 6 (b). The expanded information (elaborating on the two primary components of Net Position – Unexpended Appropriations, and Cumulative Results of Operations) is important, common to all or most federal entities, and is currently included in SFFAC No. 2, paragraph 84.

Revenues: DOC finds the proposed definition acceptable.

Expenses: DOC believes the definition is unclear, and has recommended revised wording in its answer to question 6 (c).

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset, but to be recognized, the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

DOC Response to 1 (c):

Yes, DOC agrees that if an item meets the definition of an asset, it should be considered an asset even though it would not be recognized on the financial statements. A definition of an asset must not take into account its eventual financial statement treatment. For example, assets, even if immaterial to an agency's financial statements, are normally identified and recorded in an agency's general ledger (subject to the agency's capitalization threshold.) It is important to other financial and management controls to identify assets regardless of its financial statement treatment.

Related to this question, we also agree with the proposed Concepts Statement, paragraph 9, which states, "...Unrecognized elements are candidates for disclosure in the notes to financial statements or as supplementary information."

- 2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets*, *liabilities*, *net position*, *revenues* and *expenses*. (See paragraphs 2, 3, 35-37, and 56.)
 - a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

DOC Response to 2 (a):

DOC believes that, consistent with FASAB standards (SFFAS No. 7 and SFFAS No. 21), there are two additional elements of accrual-basis financial statements for federal entities – a) Other Financing Sources (the word Other is used in SFFAS No. 7 to distinguish this from revenues); and b) Prior Period Adjustments. Both of these categories are different in important ways from the five proposed elements. DOC believes it is of significant benefit to readers of federal financial statements to continue to treat Other Financing Sources and Prior Period Adjustments as distinct categories in federal financial statements.

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

For example, Appropriations Used, and Imputed Financing, are unique and substantially different than traditional revenue reported on a financial statement.

Due to time constraints of DOC, we are not proposing the essential characteristics of these recommended additional elements at this time.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

DOC Response to 2 (b):

For recommended additional elements, see answer to 2 (a).

DOC believes that the framework provided by the five proposed elements and the two additional recommended elements are sufficient to address unique items such as long-term social insurance obligations and other commitments.

DOC believes that any information that is important to a financial statement reader but does not fit within the definition of the proposed/recommended elements may be candidates for disclosure in the financial statement footnotes or in supplementary information.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page 29)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

DOC Response to 3 (a):

DOC agrees with the position taken in the proposed Concepts Statement. DOC believes that financial reports should be based on all relevant information that exists at that time, within the context and constraints of existing conditions and current law. DOC believes that any changes in conditions or current law that affect financial reporting should be dealt with at such time when the conditions or law changes.

DOC concurs with SFFAC No. 2, paragraph 84, which states "...Also, because the Federal Government is a sovereign entity, it can abrogate at any time many of its liabilities arising from other than contracts. This does not, however, eliminate the existence of, and therefore the need to report, liabilities incurred by the reporting entity." DOC, therefore, is concerned with the alternative view that the government's power to modify the law to change or withdraw future benefits may sometimes preclude recognition of a liability. DOC believes that a liability should be recorded based on current conditions and current law.

- 4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to all federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)
 - a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

DOC Response to 4 (a):

DOC agrees with the two essential characteristics of assets proposed in the Concepts Statement.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

DOC Response to 4 (b):

DOC is not aware, at this time, of any additional characteristics that are fundamental or essential to all federal government assets.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)
- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

DOC Response to 5 (a):

“Present Obligation” Essential characteristics:

Dramatic Expansion of the Definition of Liability:

The last sentence of Exposure Draft paragraph No. 41 states the following, “A present obligation is incurred when the government takes a specific action that commits or binds the government and affects another entity.”

This sentence dramatically expands the definition of a liability, most notably to include undelivered orders (i.e. purchase orders, contracts, memoranda of agreement/understanding) and possibly commitments where goods or services have not yet been received or where the underlying event has not yet taken place. This definition of a liability is entirely inconsistent with traditional accrual-basis accounting for liabilities including accrual-basis accounting for liabilities as currently defined by FASAB in SFFAC No. 2, paragraph 84 and SFFAS No. 5, paragraph 19, and as defined by the Financial Accounting Standards Board (FASB), and as defined by the Governmental Accounting Standards Board (GASB). An undelivered order or commitment, while being a

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commitment of the government, should not be a liability (amount owed) of the government because the providing entity has not yet met its commitment or the underlying event has not yet taken place. The existence of a Federal liability is contingent upon the providing entity adequately providing the goods/services or the underlying event taking place. Until the providing entity adequately provides the goods/services or the underlying event takes place, the Federal Government is not liable to pay for those goods/services or items required as a result of the underlying event taking place (i.e. no amount is owed).

DOC is concerned about this dramatic expansion of a liability, because DOC believes that (consistent with private sector and state/local practice) readers of financial statements expect liabilities to be amounts owed by the government for goods/services received or underlying events that have taken place. To have liabilities include, for example, undelivered orders and possibly commitments, may cause liabilities as reported on the Balance Sheet to be not meaningful or useful information to readers. The Balance Sheet would include items not owed (i.e. the goods/services have not been received, so nothing is owed) as liabilities of the federal entity, and this may not be useful information that readers of financial statements would expect to see reported as a Balance Sheet "liability."

In layman's terms, DOC believes that most readers of financial statements understand "liability" to be an amount "owed," and, an undelivered order, for example, would not generally be considered an amount "owed." as the exchange of value in exchange for a promise of future payment has not yet taken place.

The federal government's definition of a liability would not be consistent with the private sector and state/local accounting for liabilities.

The reason or benefit of this significant departure from established practices across the country for accrual-basis accounting has not been explained or justified by FASAB in the Exposure Draft, in a transmittal letter, in other materials posted to FASAB's website, or otherwise.

"Present Obligation" Definition Should Include "Probable:"

DOC believes that the "present obligation" essential characteristic needs to state that the present obligation be "probable," consistent with SFFAS No. 5, paragraph 19 (see below) and FASB accrual-basis accounting for liabilities.

SFFAS No. 5, paragraph 19: "A liability for federal accounting purposes is a probable future outflow or other sacrifice of resources as a result of past transactions or events. General purpose federal financial reports should recognize *probable* and measurable future outflows or other sacrifices of resources arising from (1) past exchange transactions, (2) government-

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related events, (3) government-acknowledged events, or (4) non-exchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date.”

FASB: “Probable future sacrifices of economic benefits arising from present obligation of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions and events.”

This dramatic expansion of the definition of “liability” may cause the liability recognition of many new items that do not reach the definition of “probable” and may threaten important qualitative characteristics of reporting such as relevance, reliability, cost versus benefit, and representational faithfulness.

If “probable” is omitted from the definition of a liability, the federal government’s definition of a liability would not be consistent with the current FASB definition and would not appear to be consistent with the proposed GASB definition clause “with little or no discretion to avoid.”

The reason or benefit of this significant departure from established practices across the country for accrual-basis accounting has not been explained or justified by FASAB in the Exposure Draft, in a transmittal letter, in other materials posted to FASAB’s website, or otherwise.

“Settlement” Essential Characteristic

DOC believes that “settlement” is not an essential characteristic of a liability. If there is no agreement on when a liability will be paid, DOC believes that the liability still exists (i.e. the amount is still owed regardless of whether agreement or settlement has been reached or not.)

With regard to a situation when the government is free to decide whether to settle the obligation, DOC agrees with SFFAC No. 2, which states “...Also, because the Federal Government is a sovereign entity, it can abrogate at any time many of its liabilities arising from other than contracts. This does not, however, eliminate the existence of, and therefore the need to report, liabilities incurred by the reporting entity.” DOC believes that a liability should be recorded based on current conditions and current law.

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- b) Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities?

DOC Response to 5 (b):

DOC believes that the “present obligation” essential characteristic regarding “probable” should remain in the definition of Liability as currently stated in SFFAS No. 5 (see answer to 5 a.)

6. As indicated in Question 1a), the first principle of the Board’s approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.
- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

DOC response to 6 (a):

DOC believes that the definition of assets adequately conveys the essential characteristics of assets.

DOC believes that the definition of liabilities in SFFAS No.5 is superior to the definition shown in the Exposure Draft, and that the definition of Liability in the Exposure Draft is a dramatic expansion of the definition of a Liability that has not been adequately explained or addressed (i.e. its benefits, its purpose) by FASAB in the Exposure Draft, in a transmittal letter, in other materials posted to FASAB’s website, or otherwise (please also see answer to question 5.)

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

DOC response to 6 (b):

Net Position Definition:

No. The definition for net position described in SFFAC No.2 paragraph No.84 includes a more precise definition which elaborates on the primary components of Unexpended Appropriations and Current Results of Operations as follows: “Net position is the residual difference between assets and liabilities. It is generally composed of unexpended appropriations and the cumulative results of operations. Included in the former would be appropriations not yet obligated or

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expended, including undelivered orders. Included in the latter would be the amounts accumulated over the years by the entity from its financing sources less its expenses and losses, which would include donated capital and transfers in the net investment of the Government in the reporting entity's assets; and an amount representing the entity's liabilities for such things as accrued leave, credit reform subsidies, and actuarial liabilities not covered by available budgetary resources."

Revenue Definition:

DOC substantially agrees with the Exposure Draft definition of Revenue.

Expense Definition:

DOC believes that the definition of expense is very unclear, and respectfully recommends the following rewording: "An expense is a decrease in assets, an increase in liabilities, the consuming or adjusting of assets, or a combination of the above from the receipt of goods or services or any other activities during the reporting period."

7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

DOC response to 7 (a):

DOC is not aware, at this time, of any other criteria that should be established as conditions for recognition.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework

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permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

DOC response to 8 (a):

DOC agrees with the Alternative View that the proposed concepts statement should explicitly state that "the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability")." DOC believes that this assessment of the probability of an item meeting the definition of an element is an important step in any evaluation of an item's element.

DOC disagrees with the Alternative View that the Proposed Concept Statement should state that "there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards." DOC believes that federal entities should have the latitude to exercise their judgment in determining if it is probable or not probable that an item meets the definition of an element.

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9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 26.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

DOC response to 9 (a):

DOC agrees with the Alternative View that the proposed Concepts Statement should explicitly state that “the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurable probability”).” DOC believes that this assessment of the probability of an item being measurable is an important step in any evaluation of an item’s measurability.

DOC disagrees with the Alternative View that the proposed Concept Statement should state that “there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards.” DOC believes that federal entities should have the latitude to exercise their judgment in determining if it is probable or not probable that an item is measurable.

Department of Commerce Responses to Exposure Draft Questions Regarding Definition and Recognition of Elements of Accrual-Basis Financial Statements

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page 27.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

DOC response to 10 (a):

DOC agrees with the Alternative View regarding the consideration of the six qualitative characteristics of financial reports when determining if an item should be recognized in a financial report (i.e. meets the recognition criteria.) The six qualitative characteristics of financial reports are important to federal entities’ financial reporting, and if the recognition of an item in a financial report is not consistent with one or more of these characteristics, then that should be considered when determining if an item should or should not be reported in a financial report.

#24 – Ian Mackintosh, Non- Federal - Other

>>> "Ian Mackintosh" <imackintosh@frc.org.uk> 8/7/2006 11:10 AM >>>
Dear Wendy

Thank you for the letter from David Mosso dated June 13 2006.

I have read your document with interest. I do not propose to comment in detail or to answer your detailed questions, but to only raise a few basic points. I must stress that my comments are personal and do not necessarily reflect the views of the ASB or its staff.

Definition of an asset

I worry about the word "can" in the definition and would prefer "can control" be replaced with "controls". I am concerned that if you refer to items that the government can control this would give rise to assets that it does not presently control but could in the future if it wanted to. Given the power of the federal government to legislate, this could give rise to a large number of assets. Paragraph 33 of the document indicates that you do not really intend this outcome.

Definition of a liability

I was wondering why you need the words "at a determinable date, when a specified event occurs, or on demand" in the definition. They do not seem to add anything. In paragraph 45 you say that if the government can determine *whether* and when the liability can be settled it is not a liability. I agree, but would add that the word *whether* is very important here. If you can decide whether you will pay, you do not have a present obligation.

Definition of revenue and expense

The IPSASB definition of revenue is "the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners". Definitions from other countries are similar. I was wondering whether you could refer to an increase in net position rather than increases or decreases in assets and liabilities and then having to exclude borrowings.

Alternative views

Generally I am not in agreement with the alternative views.

Congratulations on a very good document.

Regards

Ian

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#25 – Office of Personnel Management – Office of the Inspector General, Michael Esser, Assistant Inspector General for Audits, Federal – Auditor

>>> "Esser, Michael R" <Michael.Esser@opm.gov> 8/7/2006 11:43 AM >>>

Please find our comments on the Exposure Draft on the Definition and Recognition of Elements of Accrual-Basis Financial Statements in the attachment. We appreciate the opportunity to comment on such drafts.

Thank You

Michael R. Esser

Assistant Inspector General for Audits

OPM-OIG

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1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities. **Yes. Definitions as stated in paragraphs 3, 19, 21, 40, and 49 are sufficient.**
- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses? **Yes. Definitions as stated in paragraphs 3, 19, 21, 40, and 49 are sufficient.**

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position. **Yes, it is**

an asset. Agree with paragraphs 4,6 and 9 as written; however, we agree with the Alternative Views that were stated in regards to paragraph 5 and 8

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues and expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them? No

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements. Disagree; there are no additional elements that need to be defined. Items, such as the examples given, would fall as subset under assets, liabilities, etc. as stated in paragraph 56.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of

the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position. [Agree with the proposed Concepts Statement. The liability should be recognized when it becomes a present obligation. If the law and/or circumstances change and it affects the liability, then the amount can be adjusted and/or written off as appropriate, in accordance with standards.](#)

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)
 - a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics. [Yes](#)
 - b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets? [No](#)
5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)
 - a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics. [Agree](#)
 - b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities? [No](#)
6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.
 - a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions? [Yes](#)
 - b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions? [Yes](#)
7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The

item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete? [Paragraph 4 as written is fine; however, we agree with the Alternative View regarding paragraph 5 that is stated on page 25](#)
8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page .)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position. [Agree with the Alternative View concerning the need for an explicit requirement. As stated in A8 on page 27, it would increase the “consistency” of implementation of this concept by federal agencies.](#)
9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence,

an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable ("measurability probability"), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position. [Agree with the Alternative View concerning the need for an explicit requirement. As stated in A8 on page 27, it would increase the "consistency" of implementation of this concept by federal agencies.](#)

- 10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that "Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability." These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.
[Agree with the proposed Concepts Statement and the members' rationale for not repeating the characteristics in this document.](#)

#26 – Greater Washington Society of CPAs, Federal Issues and Standards Committee, Dan Kovlac, FISC Chair, Non-Federal – Other



**Greater Washington Society of CPAs
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August 7, 2006

Wendy Comes, Executive Director
Federal Accounting Standards Advisory Board
Mail Stop 6K17V
441 G Street, NW – Suite 6814
Washington, DC 20548

Dear Ms. Comes:

The Greater Washington Society of Certified Public Accountants (GWSCPA) Federal Issues and Standards Committee (FISC) appreciates the opportunity to provide comments on the Federal Accounting Standards Board's (FASAB) Exposure Draft DEFINITION AND RECOGNITION OF ELEMENTS OF ACCRUAL-BASIS FINANCIAL STATEMENTS dated June 7, 2006.

FISC consists of 18 GWSCPA members who are active in accounting and auditing in the Federal sector. This comment letter represents the consensus comments of our members.

Responses to Request for Comments – Page 4 of ED follow:

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Yes.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Yes. However, we believe that Cumulative Results of Operations and Unexpended Appropriations should be discussed as components of Net Position.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Yes. An example might be a lawsuit that has been won, but no amount has been determined.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets*, *liabilities*, *net position*, *revenues* and *expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and

what are their essential characteristics? Alternatively, what are they and how would you define them?

Yes. Unexpended Appropriations (UA) and Cumulative Results of Operations (CRO) are components of Net Position that should be considered Elements of Net Position. Additionally, Appropriations, Other Financing Sources (OFS), Transfers In (TI), and Transfers Out (TO) are key elements in Federal financial statements and should be considered Elements.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Yes. See answer to 2.a above.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may

preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement because it accounts for current circumstances. If circumstances change (i.e. the law changes) then, that change should be accounted for at the time of the change.

- 4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Yes.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

No.

- 5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

We disagree. The definition should be changed to reflect the concept described in paragraph 46. Without this clarification, the government may not record certain obligations because there is no “agreement or understanding as to when settlement of the obligation is to occur.” In fact, the amount of the obligation may not be definite. An example would be a contingent liability that is probable of loss, but no settlement date or amount has been established.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?

No.

6. As indicated in Question 1a), the first principle of the Board’s approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

No. See answers to questions 5.a and 5.b above.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

We believe the definitions for revenues and expenses should be clarified. As these definitions are currently written in paragraphs 52 and 53, one could conclude that revenues includes transfers in, and expenses includes transfers out. We also believe that UA, CRO, Appropriations, OFS, TI, and TO should also be considered Elements and defined.

7. The proposed concepts statement establishes two conditions (“recognition criteria”) that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

See answer to question 5 above.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

We agree with the proposed Concepts Statement. “Probability” is implicit in determining an asset and liability. It is judgmental and should not be subject to a formula.

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly

discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable ("measurability probability"), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. See the answer to question 8 above.

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that "Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability." These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item

meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views.)

- b) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. The characteristics are implied and do not need to be repeated.

Other Comments

As noted above, Appropriations, Other Financing Sources, Unexpended Appropriations, Cumulative Results of Operations, Transfers In, and Transfers Out should be considered Elements and should be discussed in paragraphs 2 and 3.

Paragraph 15 addresses Appropriations. However, the paragraph says that "...a component entity would recognize appropriations as increases in assets and revenues..." Like Revenues, Appropriations increase assets. It is inconsistent to call "Revenues" an Element, but not Appropriations. The paragraph concludes by saying, "Therefore, appropriations recognized by component entities are eliminated in the process of consolidation and are not reported in the consolidated financial statements of the federal government." The fact that Appropriations do not appear in the consolidated financial statements should not prohibit appropriations from being considered Elements. They are an integral part of the component entities' financial statements, and in many cases, one of the largest amounts in the financial statements.

Paragraph 38 does not adequately consider all liabilities. The definition should be expanded to include the discussion in paragraph 46. Currently, contingent liabilities would not be covered by the definition in paragraph 38.

Paragraph 49 should be expanded to include a discussion of Appropriations and Other Financing Sources as Elements.

Paragraph 50 should be expanded to include a discussion of the components of Net Position: Cumulative Results of Operations and Unexpended Appropriations. Net Position is more complex than "the difference between the total assets and total

liabilities...” We do not agree with the statement in paragraph 51 that “a discussion of the meaning of the government’s or a component entity’s reported net position is beyond the scope of this Concepts Statement.” These are integral Elements of Net Position and should be addressed in this Concepts Statement.

A discussion of Appropriations, Other Financing Sources, Transfers In, and Transfers Out should be presented in the section currently titled “Definitions of Revenues and Expense” on page 22. The section title would also have to be changed.

In paragraphs A1 and A7, it would be helpful to the reader if examples of these situations were presented.

Note 12, on page 27, needs to be clarified. It is unclear how much the liability referred to in the last sentence of the note that might be recorded would be. Would it be for the full amount, since the probability is greater than zero, or would it be for \$100 (10% of \$1,000)? Under current standards, this would be considered remote and there would be no question as to the liability amount.

In item 3 on page 28, we do not agree with the concept that “an item need not be recognized if the costs from doing so (making an estimate) exceeds the benefit.”

On page 29, the “expected value approach” is mentioned. This should be defined in the Glossary on page 30.

On page 39, we question the need to have the work “present” in the definition of a liability. A contingent liability would not meet this definition.

This comment letter was reviewed by the members of FISC, and represents the consensus views of our members.

Very truly yours,



Daniel L. Kovlak
FISC Chair

#27 – Department of Labor, Office of the Inspector General, Mike McFadden, Director – Office of Accountability Audits, Federal - Auditor

August 8, 2006

Dear Ms. Comes:

Attached are DOL OIG comments on the subject Exposure Draft. We appreciate the opportunity to provide comments. If you have any questions regarding our comments, I can be reached at 202-693-5164.

Mike McFadden
Director, Office of Accountability Audits

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the Federal Government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

DOL OIG Response: We believe assets and liabilities should be defined by their fundamental or essential characteristics. The Statements on Federal Financial Accounting Standards (SFFAS) use fundamental and widely known accounting theory to define assets and liabilities. The SFFAS also provide specific requirements when Federal entities should recognize and report an asset or liability. We believe this Concept's definition of assets and liabilities would be consistent with the Standards.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

DOL-OIG response: We believe the Concepts Statement should derive the definitions of net position, revenue and expense from assets and liabilities.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

DOL-OIG Response: We agree that an item that meets the definition of an asset is an asset even if it is not recognized with a value in the financial statements. We agree with the Concepts Statement recognition criteria, that an asset must be measurable to be recognized and that immaterial items need not be recognized as assets in the financial statements. Federal agencies own and maintain a number of items where they are not required by Federal Accounting Standards to report a value on the balance sheet. We believe that if items meet the definition and recognition criteria in this Concepts Statement, they should be recognized. This may require changes to Federal Accounting Standards to ensure they are aligned with this Concepts Statement.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets*, *liabilities*, *net position*, *revenues* and *expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

DOL-OIG Response: The Concepts Statement addresses only the proprietary side of the accrual-based financial statements and excludes the budgetary resources that make up Federal financial statements. We believe that the statement should also make reference to budgetary accounts since budgetary reporting is required in Federal Financial Statements. For example, the Concepts Statement could define the major sections of the Statement of Budgetary Resources (Budgetary Resources, Status of Budgetary Resources, and Relationship of Obligations to Outlays) and the Statement of Financing. Alternatively, the Concepts Statement could refer to OMB Circular A-11, Part 4 for these definitions.

Some constituents believe that because of the unique nature of the Federal Government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

DOL-OIG Response: We strongly disagree that FASAB should include additional elements for certain unique transactions and events. While there are a number of unique transactions and events in the Federal Government, these unusual transactions and events will meet the criteria for one of the defined elements. They may need to be specifically identified or disclosed in the financial statements, but those differences in presentation are covered by the Standards and should not be dealt with in this Concepts Statement. While these unique transactions and events may be reported separately, they still should be

recognized in the financial statements in accordance with one of the defined elements contained in this Concepts Statement.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the Federal Government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the Federal Government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the Government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44.

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

DOL-OIG Response: We strongly agree with the position taken in the proposed Concepts Statement concerning the potential effect of the government's ability to change laws on the recognition of a liability. If and until the Government changes the law, the financial statements should reflect the current state of affairs. OMB Circular A-136 specifically requires Federal agencies to disclose the Government's ability to change laws on the recognition of a liability within the summary of significant policies of the financial statement footnotes. This footnote clearly discloses the Government's ability to change law and we believe no additional discussion is needed in the Concepts Statement.

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* Federal Government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)
 - a) Do you agree that these two characteristics are essential characteristics of all Federal Government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

DOL-OIG Response: We agree that the two characteristics are essential for all Federal Government assets.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to all Federal Government assets?

DOL-OIG Response: We did not identify any additional characteristics that are fundamental and essential to all Federal Government assets.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to all Federal Government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the Federal Government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all Federal Government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

DOL-OIG Response: We agree that the two characteristics are essential for all Federal Government liabilities.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to all Federal Government liabilities?

DOL-OIG Response: We cannot identify any additional characteristics that are fundamental and essential to all Federal Government liabilities. We believe, however, that FASAB should use the Concept's statement to address inconsistencies within the SFFAS. For example, the DOL is required to recognize an actuarial liability for the FECA program. Under SFFAS No 17, DOL is only required to recognize the current year liability for the Black Lung Program. This treatment is inconsistent since the population is known for both programs and an actuarial estimate can easily be made.

6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

DOL-OIG Response: We believe the Concepts Statement does adequately define and convey the essential characteristics of assets and liabilities.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

DOL-OIG Response: We believe that the Concepts Statement conveys the relationship of net position, revenues and expenses to the associated assets and liabilities.

7. The proposed Concepts Statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The

item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

DOL-OIG Response: We did not identify any other criteria the FASAB should establish as a condition for recognition.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities

- b) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

DOL-OIG Response: We disagree with the Alternative View concerning the need for an explicit requirement. An explicit requirement to assess the probability and the related probability threshold could have the effect of reducing the use of management judgment of whether they believe items should or should not be recognized as part of these elements.

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities.

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

DOL-OIG Response: We disagree the Concepts Statement should explicitly state the probability that an item is measurable and where the threshold exists for that item to be measurable. An explicit requirement would only take into consideration the quantitative characteristics for each measurable item. Management should also take into account the qualitative characteristics of each reported line item as well. Line items not quantitatively material could have qualitative aspects requiring that they be reported in the financial statements.

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item

meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

DOL-OIG Response: We disagree with the Alternative View that qualitative characteristics should be considered in determining whether management should recognize an item in the financial statements. The characteristics in SFFAC 1 relate to the statements taken as a whole. We don't believe these necessarily relate to whether or not individual components are recognized in the financial statements.

**#28 – Department of Defense, Terri McKay, Deputy CFO, Federal –
Preparer**



COMPTROLLER

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AUG 10 2006

Ms. Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

Comments from the Department of Defense on the Federal Accounting Standards Advisory Board (FASAB) Exposure Draft for the proposed Statement of Federal Financial Accounting Concepts, *Definition and Recognition of Elements of Accrual-Basis Financial Statements* are enclosed.

The Department appreciates the opportunity to comment on the Exposure Draft. My staff point of contact is Ms. Regina Kearney. She may be reached by email at regina.kearney@osd.mil or by telephone at (703) 697-6149.

Sincerely,

A handwritten signature in black ink, appearing to read "T. McKay", is written over a horizontal line.

Teresa McKay
Deputy Chief Financial Officer

Enclosure:
As stated

**Definition and Recognition of Elements of
Accrual-Basis Financial Statements
FASAB Exposure Draft
June 7, 2006**

- 1.A** Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Response: The definitions of assets and liabilities should be derived from their fundamental or essential characteristics. Capturing the fundamental characteristics of what constitutes an asset or liability will result in a more accurate interpretation of what is an asset and what is a liability by providing useful guidance for determining how to classify an item.

- 1.B** Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Response: The definitions of net position, revenue and expenses should derive from the definitions of assets and liabilities. The inflows and outflows of an entity are a direct result of the management of the assets and liabilities as they relate to the production of goods or services of the entity.

- 1.C** If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Response: We agree the concept of definition and recognition should be separated. If an item meets the definition of an asset and holds the characteristics of an asset, it is an asset even if it is not recognized in the body of a financial statement. Uncertainties around measurability or materiality do not change the nature of the item.

- 2.A** Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Response: We believe the fundamental difference stemming from transactions that are within the course of business vice something unusual, warrants having its

own definition. Therefore gains and losses although they could be construed as the same as revenues and expenses, should be separately defined.

- 2.B** Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Response: Yes, additional elements do need to be defined. As stated in 2.A, gains and losses should be defined.

- 3.A** The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on existing conditions, including current law, because an essential characteristic of a liability is that the government has a present obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page 29.)

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Response: We agree with the proposed Concepts Statement and do not agree with the Alternative View. Our financial statements are representations of the financial condition of the government from a specific point in time. In order to be useful

and reliable it is necessary to produce these statements based on current law, not on the possibility of a law changing in the future. Financial statements should provide the information needed to assess whether current law needs to be modified. In addition, adopting the alternative view approach could have adverse effects on many items other than social obligations. Many current liabilities are estimates based on current law, which will possibly change in the future, such as environmental liabilities. Proposing that such items may not be an obligation because a law may change in the future could result in an increase in off-balance sheet liabilities. Additionally, there are a number of things the government could do to eliminate their responsibility for liabilities, even if the probability of such action is, at best, remote (change laws, conquer nations, incarcerate individuals, simply refuse to acknowledge the debt). Shall we then remove all liabilities from the Balance Sheet based on these unforeseen events? Furthermore, this alternative concept could be applied to assets as well as liabilities, in that the government has the power to claim assets and resources that could result in misrepresentation if there is no basis of a past event or transaction that results in the ability to recognize the asset or resource.

- 4.A** The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Response: Yes, these two characteristics are essential characteristics of all federal government assets.

- 4.B** Are there any additional characteristics that are fundamental or essential to all federal government assets?

Response: There are no additional characteristics that are fundamental or essential to all federal government assets.

- 5.A** The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Response: We believe the current definition in SFFAS 5 & SFFAS 6 and the proposed definition adequately define federal government liabilities. The current definition requires the liability to be based on a present obligation and to have a settlement date. The proposed definition in connection with the proposed recognition criteria considers probability in definition and measurement of liabilities.

- 5.B** Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

Response: There are no additional characteristics that are fundamental or essential to all federal government liabilities.

- 6.A** Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Response: The definitions of assets and liabilities adequately convey their characteristics.

- 6.B** Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Response: The definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

- 7.A** The proposed concepts statement establishes two conditions (“recognition criteria”) that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

Response: There are not other criteria that should be established as conditions for recognition.

- 8.A** The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the existence of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for recognition, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

Response: When determining whether an item meets a definition of an element of the financial statements, professional judgment will be used. We do not have an issue with explicitly requiring this in the concept; however we believe probability

considerations are inherent to defining an element and the explicit statement is not necessary.

- 9.A** The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57- 61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 26.)

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

Response: When determining whether an item is measurable, professional judgment will be used. We do not have an issue with explicitly requiring this in the concept; however we believe probability considerations are inherent to measuring an element and the explicit statement is not necessary.

- 10.A** SFFAC 1, Objectives of Federal Financial Reporting, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members

supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page 27.)

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position

Response: Qualitative characteristics, as covered in SFFAC 1, are a consideration underlining the financial statements. Paragraph 1 of the proposed concepts states this concept is consistent with earlier Concepts. Re-stating the qualitative characteristics in the proposed concept would greatly reduce confusion of whether these characteristics are to be considered in this concept. In addition, this would enhance reader ease.

#29 - Department of Treasury, James R. Lingeback, Director of Accounting and Internal Control, Federal – Preparer



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220
August 14, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
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441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

Thank you for the opportunity to provide comments on the June 7, 2006 exposure draft (ED) titled "Definition and Recognition of Elements of Accrual-Basis Financial Statements – *Proposed Statement of Federal Financial Accounting Concepts*." Our comments, in response to the questions on page four of the ED, are as follows:

1. 1a. Question: Should the definitions of assets and liabilities derive from their fundamental or essential characteristics?

Response: Yes. We believe assets and liabilities should be defined based on their essential characteristics. In reviewing FASB Concept No. 6, we also believe that this provides an excellent definition, and suggest that they be compared to make certain that our FASAB Concept Statement is congruent.

- 1b. Question: Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities?

Response: Yes. We also believe that there should be a further definition of net position to include cumulative results of operations and unexpended appropriations.

- 1c. Question: If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Response: Yes. We agree with the proposed concept, and agree that an item can meet the definition of an asset, even if it is not measurable or is not recognized because of materiality. An entity such as the Federal government can be expected to have assets for which a cost or market value is not readily determinable, but is nonetheless important to the overall understanding of the financial statements.

2. 2a. Question: Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Response: We believe that the following elements should also be defined in the Concepts Statement:

1. Unexpended Appropriations
2. Cumulative results of Operations
3. Appropriations
4. Other Financing Sources
5. Transfers In
6. Transfers Out

These are unique elements of our statements that warrant separate definitions in the overall context of the Concepts Statement.

We also believe that existing differences with accrual basis financial statements and cash basis budgetary statements should be considered in the definition of elements. It is important for readers to understand the distinctions.

2b. Question: Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements?

Response: see response for 2a.

3. 3a. Question: Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Response: We agree with the proposed Concepts Statement because it reflects the current law and legal requirements, not the alternative view.

4. 4a. Question: Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Response: We agree with the proposed Concepts Statement.

4b. Question: Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

Response: No additional characteristics.

5. 5a. Question: Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Response: We agree with the characteristics.

5b. Question: Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities?

Response: We have none.

6. 6a. Question: Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Response: We agree with the definition.

6b. Question: Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Response: We believe that the following elements should also be defined in the Concept:

- 7. Unexpended Appropriations
- 8. Cumulative results of Operations
- 9. Appropriations
- 10. Other Financing Sources
- 11. Transfers In
- 12. Transfers Out

We also believe that existing differences with accrual basis financial statements and cash basis budgetary statements should be considered in the definition of elements.

(See response to question 2.a. above.)

7. 7a. Question: Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

Response: We have no other criteria.

8. 8a. Question: Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element?

Response: We agree with the position taken in the proposed Statement and do not believe its adoption will result in many more items being recognized. While we agree that there may be an implicit assessment of probability, we do not agree that thresholds should be applied. We believe explicit definitions or formulas for assessing and measuring probability run the risk of excluding many more items from recognition.

Furthermore, we suggest a review of FASB Concept No. 6 paragraph 25, and especially footnote 18 which states "Probable is used with its usual general meaning, rather than in a

specific accounting or technical sense.” We do not believe that the FASAB Concept Statement should imply otherwise.

9. 9a. Question: Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable?

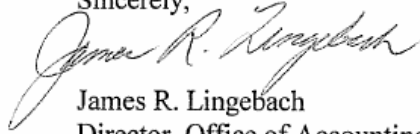
Response: We agree with the position taken in the proposed Statement for the same reason as stated on 8 above.

10. 10a. Question: Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

Response: We agree with the position taken in the proposed Statement. We do not believe that failure to include the qualitative characteristics will result in erroneous recognition and agree that repeating the qualitative characteristics runs the risk of causing confusion about their application.

Again, we appreciate the opportunity to comment on this exposure draft. If we can be of further assistance, please contact me on (202) 622-0818, Joseph McAndrew on (202) 622-0807, or Don Geiger on (202) 622-0809.

Sincerely,



James R. Lingeback
Director, Office of Accounting
and Internal Control



Office Of Inspector General

August 2, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Comes:

In response to the President's Council on Integrity and Efficiency's June 7, 2006, request for comments on the Federal Accounting Standards Advisory Board's (the Board) Exposure Draft, Definition and Recognition of Elements of Accrual-Basis Financial Statements, we submit the following comments to the exposure draft questions:

Question 1: Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government. The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics?

We concur that the definitions of assets and liabilities should derive from their fundamental or essential characteristics. As the role and functions of governmental entities evolve and change (for example the legislation which resulted in entitlement programs in the 1900's), so will the transactions which support the elements of accrual based financial reports. The definitions of assets and liabilities should be as general as possible to allow the practitioner and/or entity to determine how each transaction should be classified and reported, if at all, in the financial statements through prudent professional judgment.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities?

The definitions of net position, revenues and expenses should derive from the definitions of assets and liabilities as these income statement or

statement of activities accounts are used to record the inflow and outflow of assets and the accumulation or relief of liabilities. By deriving these definitions from the balance sheet accounts, it reinforces the relationships between the accounts and financial reporting statements. Also, that is the process used by the Financial Accounting Standards Board (FASB) to define the income statement accounts. When feasible, it is best to remain consistent as to keep a level of transparency between financial reports of various types of organizations and provide ease of understanding for the users of governmental financial statements.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, *meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements.* An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material?

An item that meets the definition of an asset is an asset even if it is not reportable due to inability to measure the asset or due to immateriality. An asset, even if not material, can provide future economic benefit to the entity. Also, the inability to measure an asset does not decrease its value to the entity. For example, in government which is not strongly based in the production or delivery of goods, more value is placed on processes and human capital to influence the delivery of services to the various stakeholders of governmental entities. While much debate has been raised about how to place a value on human capital and present it in the financial statements, no agreement has been reached. Although not represented in the financial statements, the loss of human capital could severely hamper the ability of an entity to provide services to its stakeholders and achieve its mission. As such, it is clear that an item not presented in the financial statement can still provide future economic benefit to the entity which has control over the item.

In regard to an item being categorized as an asset which is not material, there is not a one to one ratio of the value of an asset and the ability to generate economic benefit. An item may generate benefits many times greater than the value of the item. Also, misuse of an item, entrusted for use by an entity to achieve its mission, while immaterial may present a material risk if it is perceived by stakeholders that the items are being misused.

Question 2: The proposed Concepts Statement defines five elements of accrual-basis financial statements: assets, liabilities, net position, revenues and expenses. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Although FASB guidance contains additional elements, at this time, we concur that the five aforementioned elements are sufficient.

- b) Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement. Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements?

We disagree that there are additional elements that need to be defined at this time. The FASB provides for accounting for intangible resources and long term liabilities which can be classified, measured and are probable. Anything outside of that would be an attempt to quantify the mission of the government on the face of the financial statements, which would hamper the comparability of statements from entity to entity as they may have different missions and different items represented in the financials. And while government financial reporting is different from commercial or not for profit financial reporting, it should not become so different as to create a whole new system of financial reporting and eliminate transparency from the financial reporting process so that only those with expertise in governmental financial reporting can understand the financial statements of reporting entities. Consideration for additional elements could occur later.

Question 3: The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on existing conditions, including current law, because an essential characteristic of a liability is that the government has a present obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be

able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page **Error! Bookmark not defined..**)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. The balance sheet is a point in time picture of assets, liabilities and net position as of a given day. All entities (government and commercial) face the possibility of change in the value of assets and liabilities due to changes in the environment. The COSO model, integrated in government financial reporting through the Government Accounting Office's use of it in providing standards for internal control in governmental financial reporting, clearly requires consideration of regulatory factors in measurement and reporting of transactions through the financial statements. Due to the sweeping ability of government to change laws and effect future obligations, discussion of such items would make the financial statements only slightly representative of the future obligations of a component entity's obligations of as a particular date. The balance sheet and income statement should provide as comprehensive an outlook of the net position and activities of an entity as possible as of a given point in time and period. Also, the alternative view would require one to place probabilities on changes in laws across large periods of time. It is highly improbable that could be done with any level of reliability as political climates and electorates change over time.

Question 4: The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

We agree. The most basic definition of an asset is as follows: An asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise. Therefore, an asset is a resource that embodies economic benefits or services that the federal government can control. Stated another way, to be an asset of the federal government, a resource must possess two characteristics. First, it embodies economic benefits or services that can be used in the future. Second, the government can control access to the economic benefits or services and, therefore, can obtain them and deny or regulate the access of other entities.

- b) Are there any additional characteristics that are fundamental or essential to all federal government assets?

We agree with the proposed Concept Statement - there are no additional characteristics that are fundamental or essential to all federal government assets.

Question 5: The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40-48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

We agree. The most basic definition of a liability is as follows: A liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits. Therefore, within the confines of the government, a liability is a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand. Stated another way, a liability of the federal government has two essential characteristics. First, it constitutes a present obligation to provide assets or services to another entity. Second, the federal government and the

other entity have an agreement or understanding as to when settlement of the obligation is to occur.

- b) Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

We agree with the proposed Concept Statement - there are no additional characteristics that are fundamental or essential to all federal government liabilities.

Question 6: As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Yes. The definitions of assets and liabilities adequately convey the essential characteristics from which they are derived. An asset is a resource that embodies economic benefits or services that the federal government can control. A liability is a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Yes. The definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities. Net position or its equivalent, net assets, is the arithmetic difference between the total assets and total liabilities recognized in the federal government's or a component entity's balance sheet. Net position may be positive (assets greater than liabilities) or negative (assets less than liabilities). Revenue is an increase in assets, a decrease in liabilities, or a combination of both from providing goods or services, levying taxes or other impositions, receiving donations, or any other activity (excluding borrowing) performed during the reporting period. An expense is a decrease in assets, an increase in liabilities, or a combination of both from providing cash or cash equivalents, goods or services, or any other activity (excluding repayments of borrowing) performed during the reporting period.

Question 7: The proposed concept statement establishes two conditions ('recognition criteria') that should be met for an item to be recognized in the body of a financial statement. (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there other criteria that should be established as condition for recognition? If so, what recognition criteria would you add or delete?

We agree with the following statement from paragraph #4 of the exposure draft on recognizing an element into the financial statements: "that recording not only the acquisition or incurrence of the item but also later changes in it, including changes that result in removal from the financial statements." Also, paragraph #5 of the exposure draft addresses measurability of the item: "Measurement of an item includes an assessment of the probability of future inflows or outflows of resources or services resulting from that item in a manner that is consistent with the measurement attribute being used". The above statements (along with the other statements in the exposure draft) are sufficient explanations of the recognition criteria. We disagree with the alternative view, with the explicit thresholds standards that would be applied measurability of the elements.

Question 8: The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the existence of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for recognition, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.) Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2)

there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element?

We agree with the proposed Concepts Statement that the existence of an element is judgmental, based upon available evidence. Implicit in this statement is some type of measurement as to whether or not it meets the definition of an element. Explicit standards, thresholds and existence probability proposed in the Alternative View would force federal agencies into a "one size fits all" approach to the financial statements. Additionally, it would needlessly complicate the Concepts Statement. It is sufficient to let the individual federal agencies decide, after their own judgment, whether an item possesses the characteristics of an element, and assess the probability of future inflows or outflows from the item.

Question 9: The proposed Concepts Statement defines "measurable" as "means quantifiable in monetary units." (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61) Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable ("measurability probability"), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more

items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 26.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable?

We agree with the proposed Concepts Statement. Implicit in the Concept Statement is the measurement of the probability of deciding whether an item meets the criteria for inclusion/exclusion in the financial statements. Also implicit in the Concepts statement is the consideration of a threshold at which an item is not measurable. The problem we have with the Alternative View is that some items, such as cash, may not have to be assessed as part of determining whether an item is measurable. Also, who is going to set the thresholds for the specific standards; and what are the standards to be applied? Do they evenly apply to all federal agencies? It is best left to the individual federal agencies to apply their own measurements of probability and thresholds.

Question 10: SFFAC 1, Objectives of Federal Financial Reporting, par. 156, states that "Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability." These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner. The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page 27.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a

consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

We agree with the proposed Concepts Statement. Implicit in the recognition criteria are the six characteristics of: understandability, reliability, relevance, timeliness, consistency, and comparability. These characteristics do not have to be explicitly stated in the recognition criteria. They are already explicitly stated in SFFAC1, Objectives of Federal Financial Reporting. Explicitly requiring a consideration of the six additional qualitative characteristics might create confusion and additional complexity in the recognition criteria process.

Thank you for the opportunity to comment. As requested, we are transmitting this response via email to you at comesw@fasab.gov, with a courtesy copy to Kim Geier at kim.geier@ed.gov.

If you have any questions, please contact Lorie Siewert, Director, Financial Statements, or John Cihota, Deputy Assistant Inspector General for Financial Operations, at (703) 248-2300.

Sincerely,

A handwritten signature in black ink that reads "Gordon C. Milbourn III" followed by a stylized flourish.

Gordon C. Milbourn III
Assistant Inspector General
for Audit



August 4, 2006

Mr. David Mosso
Chairman
Federal Accounting Standards Advisory Board
441 G Street NW
Mailstop 6K17V, Washington, DC 20548

Dear Mr. Mosso:

**Exposure Draft of a Proposed Statement of Federal Financial Accounting Concepts —
*Definition and Recognition of Elements of Accrual Basis Financial Statements***

Thank you for your letter dated June 13, 2006 inviting our comments on the above exposure draft. We welcome the initiative of the Federal Accounting Standards Advisory Board (FASAB) to strengthen the conceptual framework for the preparation of accrual-basis financial statements for the United States Federal Government and its component entities. The exposure draft proposes definitions of elements or “building blocks” of financial statements and the criteria for their recognition which, once finalized, should promote uniformity in the application and interpretation of accounting and reporting standards, and provide a common foundation for the preparation of future standards and the review of existing standards.

As a general comment, we would like to emphasize the importance of consistency of the framework proposed by the FASAB with related international standards. In this connection, we note that the FASAB is proposing a definitional framework that differs in several respects from *International Public Sector Accounting Standards (IPSAS)*. Admittedly, some of the differences relate to the precise wording of definitions rather than the underlying concepts. However, the wording of definitions can have a significant influence on the manner in which concepts are interpreted, and any unnecessary divergence from IPSAS should be avoided.

We would also suggest that, to the extent practical, the accounting definitions and concepts proposed should be harmonized with macroeconomic statistical standards, and in particular with the *1993 System of National Accounts* and the *Government Finance Statistics of 2001 (GFSM 2001)*. While it is recognized that the accounting and statistical bases of reporting have different objectives, they also have many similar requirements for the recognition and measurement of financial information, and for dealing with similar transactions. As you may be aware, the IMF chaired the Task Force on Harmonization of Public Sector Accounting (TFHPSA), which worked towards identifying differences between accounting and statistical

standards, promoting harmonization where possible and appropriate, and ensuring that divergences in requirements arise only where necessary.

The attached note contains our responses to the detailed questions raised in the exposure draft and highlights specific inconsistencies with *IPSAS* or *GFSM 2001*.

Sincerely yours,



Teresa Ter-Minassian
Director
Fiscal Affairs Department

Attachment

cc: Mr. Edwards
Mr. Kuhn

FASAB Exposure Draft of a Proposed Statement of Federal Financial Accounting Concepts

Definition and Recognition of Elements of Accrual Basis Financial Statements

Responses to specific questions¹

Question 1 a): Should the definitions of assets and liabilities derive from their fundamental or essential characteristics?

- We agree that assets and liabilities should be defined in terms of their fundamental or essential characteristics.

Question 1 b): Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities?

- The definitions of revenue and expenses should also be derived from their fundamental or essential characteristics and not from the definitions of assets and liabilities. The proposed definition of revenue, for example, as “an increase in assets, a decrease in liabilities, or a combination of both,” appears to confuse the *concept* of revenue, which is an inflow of (or increase in) economic benefits during an accounting period, with the *impact* of such an inflow, which is to increase the stock of assets or reduce the stock of liabilities or a combination of both. Such a reformulation of the definition of revenue and expense in terms of flows would also be consistent with *IPSAS*.
- In addition, the wording of the proposed definitions of revenues and expenses may be susceptible to misinterpretation. Contrary to *IPSAS*, the proposed definition does not make it clear that revenue should result in an *increase in the net position* of the government. Similarly, it should be indicated that expenses result in a decrease in the net position of government. It is this impact on the net position that is the essential characteristic that distinguishes revenue and expenses from the other elements of financial statements.
- Paragraphs 55 and 56 indicate that certain inflows and outflows of resources that existing standards treat as *gains* and *losses* are to be included in revenue and expense. We have two comments on this issue.
 - First, the proposed treatment is inconsistent with *GFSM 2001*, under which a distinction is made between revenues and expenses arising from transactions, and other economic flows resulting from volume and/or value changes. The policy implications of such a distinction for governments are important, given

¹ The questions are expressed in an abridged form in this document. For the full questions, reference should be made to the exposure draft.

that transactions require policy decisions while the other economic flows result from events beyond the control of policy makers. Consideration could be given to making this distinction in the concept statement to facilitate policy analysis.

- Second, the proposal to include gains and losses as part of revenues and expenses appear to be at odds with the proposed definitions of these two elements, which stipulate that they can only arise as a result of *activities performed during the period*. Other standards, for example, the *Framework for the Preparation and Presentation of Financial Statements* of the Australian Accounting Standards Board makes a distinction between *revenues and expenses*, which arise from the ordinary activities of an entity, and *gains and losses* that may or may not arise from the ordinary activities of an entity. Consideration could be given to further clarifying this issue.
- The proposed definition of the “net position” as simply the “arithmetic difference between the total assets and liabilities” fails to recognize that certain items do not satisfy the definition of asset, liabilities, revenues, or expenses and are classified separately from these four items. For example, “contribution by owners” may lead to an increase in assets, but not a corresponding increase in liabilities or revenues, or a decrease in expenses. Instead, such contributions are usually classified as an “equity” transaction. It, therefore, seems to us necessary to define “equity” (or any other term that may be considered appropriate) as a separate element in its own right, rather than one which is just the arithmetic difference between two other elements. The definition could follow the wording used in *IPSAS* e.g. equity (or other suitable word) is “the residual interest” of the federal government in its assets after deducting all its liabilities.

Question 1 c): If an item meets the definition of an asset, is it an asset even if it is not recognized in the body of financial statement?

- We agree that an item that meets the definition of an asset is an asset even if it not recognized, for example, because it is not capable of being reliably measured. We note that the exposure draft does not raise a similar question about a liability that meets the definition of a liability but is not recognized in the financial statements. The exposure draft should make the status of such liabilities clear.

Question 2 a): Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement?

- See above.

Question 2 b): Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements?

- See above.

Question 3 a): Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability?

- We agree with the position taken in (1) the proposed Concepts Statement.

Question 4 a): Do you agree that these two characteristics are essential characteristics of all federal government assets?

- We agree. However, we believe that the words "embodies economic benefits" used in the definition of assets are imprecise and could be misinterpreted. The *IPSAS* definition of an asset as "a resource from which future economic benefits are expected to flow" to the entity may be clearer.

Question 4 b): Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

- A fundamental or essential characteristic of an asset is that a "past event" must have occurred giving rise to the asset. This concept is, for example, one of the main reasons that the mere existence of the sovereign power of taxation is not considered to give rise to an asset, until a taxable event has occurred. As paragraph 33 of the exposure draft indicates, the concept of past events is implicit in the definition. However, in the absence of it being explicitly incorporated in the definition, this essential characteristic may be overlooked when considering whether particular items satisfy the definition of an asset. Incorporating the concept of past events explicitly in the definition would also be consistent with *IPSAS*.
- Paragraph 25 of the exposure draft acknowledges that the one of the main objectives of the federal government is to provide public services and that infrastructure created to provide this service should be recognized as government assets. Since infrastructure performs the function of providing public facilities, it seems anomalous to suggest, such as paragraph 31 does, that public highways should not be recognized as federal government assets. Paragraph 31 makes the point that for a highway to qualify as a government asset, the government must be able to control its use or regulate other entities' access to it. The fact that the government does not restrict access to a particular public highway does not entail that this asset is not controlled. The important point is that if it so chose, the government could restrict access to the highway—a situation that is quite different from controlling access to natural resources such as air.

Question 5 a): Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities?

- We do not agree that an agreement or understanding between the federal government and the other entity "as to when settlement of an obligation is to occur" is an essential characteristic of a liability. It is possible for two parties to agree that an amount is

owed by one party to the other, but disagree on, or be in the process of negotiations about, the timing of the settlement. Under such circumstances, there would clearly be a liability. We note that the *IPSAS* definition of liabilities does not require an agreement between the two parties.

Question 5 b): Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities?

- As with the definition of assets, discussed above, the concept of “past events” should be explicitly incorporated as part of the definition of liabilities.

Question 6 a): Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived?

- See discussion above.

Question 6 b): Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities?

- See discussion above.

Question 7 a): Are there *other* criteria that should be established as conditions for recognition?

- Incorporating as a recognition criterion the *probability* that the economic benefits associated with an item would flow from or to the reporting entity may be a compromise between the position put forward by the exposure draft and the alternative view. The exposure draft’s position is that probability is implicit in the measurement of an item but does not require to be explicitly mentioned; the alternative view is that the concept of probability should be explicitly incorporated both in deciding whether an item meets the definition of an element and whether any such element is measurable.
- Paragraph 8 of the exposure draft could give the impression that the FASAB is proposing “materiality” as a third recognition criterion. Materiality is generally viewed as one of the qualitative characteristics of financial statements, and as indicated in the response to 10 a) below, we do not believe that it is necessary or useful to repeat all the qualitative characteristics as part of the recognition criteria. The relevant text could be made clearer.

Question 8 a): Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element?

- See response to 7 a) above.

Question 9 a): Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item is measurable?

- See response to 7 a) above.

Question 10 a): Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria?

- We agree with the position taken in the exposure draft.

Other comments

Ensuring consistency between the proposed conceptual framework and the specific accounting standards has proven to be challenging for some of the Fund's members that prepare consolidated government-wide financial statements. For example, the promulgation of detailed guidance to existing standards may be required by preparers and auditors of government-wide financial statements due to the unique nature of governmental financial reporting. Therefore, we would encourage the FASAB to continue its dialogue with stakeholders, including other jurisdictions that produce full accrual-basis financial statements on a government-wide basis, to ensure that the proposed framework is consistent with existing standards.

National Aeronautics and
Space Administration

#32
Headquarters

Washington, DC 20546-0001

NASA CFO - G. Sykes Federal - Preparation



August 10, 2006

in of: Office of the Chief Financial Officer

Ms. Wendy Comes
Federal Accounting Standards Advisory Board
441 G Street NW
Suite 6814
Washington, DC 20548

Dear Ms. Comes:

The National Aeronautics and Space Administration is writing in response to the exposure draft on the proposed Statement of Federal Financial Accounting Concepts entitled *Definition and Recognition of Elements of Accrual-Basis Financial Statements*. As requested, the enclosure responds to the questions that appear on pages 4 through 9.

If you have any questions regarding this matter, please contact Mr. Jack Blair, Acting Director for Financial Management, at (202) 358-0091.

Sincerely,

A handwritten signature in black ink, appearing to read "G. Sykes", written over a light blue grid background.

Gwendolyn Sykes
Chief Financial Officer

8/29/2006

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Enclosure

- Assets and/or Liabilities must meet the definition of an element and must be recognized as measurable to be included on the financial statements. If an asset or liability is not measurable then, the asset and/or liability can be disclosed through footnotes. In addition, an Asset and/or Liability must be material. If it is not material, it should only be disclosed by footnote. Finally, the Assets and/or Liabilities must meet the definition of probable. A probability assessment and threshold must be established for inclusion in the Financial Statements to fairly represent the financial position of a Government entity.
- Only the Five elements should be included in the Concept Statement. If there are other transactions or events, these should only be disclosed through footnotes.
- The draft does not cover the elements and criteria for budgetary accounting. The discussion is exclusively from a proprietary point of view. One could infer that the definitions and criteria listed for proprietary balances would apply to the respective budgetary transactions. This, however, leaves a void for those budgetary transactions that do not have proprietary entries, such as undelivered orders (4801).
- Question 6b: Paragraph 53 describes an expense as “providing cash or goods.” It should be “receiving goods or services or paying cash or cash equivalents.”

DEFINITION AND RECOGNITION OF ELEMENTS OF ACCRUAL-BASIS FINANCIAL STATEMENTS

Questions for Respondents

The FASAB encourages you to become familiar with all proposals in this proposed Concepts Statement before responding to the questions in this section. The paragraphs cited in parentheses in a question are particularly relevant to that issue, but other portions of the document also may enhance your understanding of the question.

The Board also would welcome your comments on other aspects of the proposals in this proposed Concepts Statement. Because the proposals may be modified before a final Concepts Statement is issued, it is important that you comment on proposals that you agree with as well as any that you disagree with. Comments that include the reasons for your views will be especially appreciated.

The questions in this section are available in a Word file for your use at www.fasab.gov/exposure.html. Comments should be sent by e-mail to comesw@fasab.gov. If you are unable to respond by e-mail, please fax your responses to (202) 512-7366 and follow up by mailing your responses to:

*Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548*

All responses are requested by August 5, 2006.

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental* or *essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

NASA Response: Yes.

The definition of assets and liabilities should be derived from the fundamental or essential characteristics that all assets and liabilities respectively share.

One of the objectives of financial reporting in the federal government is to provide information about the economic resources, claims to resources, and changes in resources and claims. To meet these objectives, financial statements are prepared using basic "building blocks" or "elements". For example, the financial position of an entity is portrayed in the balance sheet by three major elements; assets, liabilities

and equity. Assets represent probable future economic benefits controlled by the entity. Liabilities represent obligations to other entities. While assets and liabilities are measured directly, equity is not. Equity is a residual amount known as net assets. This basic accounting equation is represented by Assets minus Liabilities equal Equity. So the definition of assets and liabilities, the two direct elements on the balance sheet should be derived from its essential characteristics to meet the financial reporting objectives.

In the Concepts Statement, paragraph 24 mentions tangible and intangible assets, but expanding on these items in the initial definition of asset (paragraphs 17 through 19) would provide more clarity.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

NASA Response: Yes.

The definitions of net position, revenues, and expenses should be derived from the definitions of assets and liabilities. Net position or equity is not directly measured; it is what remains when assets are reduced by the amount of obligations to creditors and others. It is a net concept. Revenues are gross inflows resulting from providing goods or services to customers, and conversely, expenses are gross outflows incurred in generating services.

The FASAB definition of revenue and expenses (paragraph 53) states “any other activity performed during the reporting period” this phrase does not add any clarity to the definition and is rather ambiguous. Considering the increase in Federal provider entities, earning and collecting revenues may warrant a more expansive definition and/or examples in the concept statement. Consider distinguishing between exchange and nonexchange revenues.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

NASA Response: Yes. We agree that once an item meets the definition of an asset, it is an asset regardless of whether it also meets the requirements to be recognized or disclosed in the financial statements.

2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues and expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

NASA Response: Statement of Financial Accounting Concept 6 (for private accounting) defines 10 elements of financial statements known as the “building blocks” with which financial statements are constructed. They are: (1) assets, (2) liabilities, (3) equity, (4) investments by owners, (5) distribution to owners, (6) revenues, (7) expenses, (8) gains, (9) losses, and (10) comprehensive income. Out of this list, investment by owners, distribution to owners, and comprehensive income are unique to private industry and not for federal government, leaving 7 elements.

The issue to be considered is whether gains and losses should be considered as additional elements. The Federal accounting system does recognize gains and loss separately from a reporting classification perspective. The U.S. Standard General Ledger structure uses 1000 series for assets, 2000series for liabilities, 3000 series for net position, 5000 series for revenue and other financing sources, 6000 series for expenses, and 7000 series for gain/losses/miscellaneous items. This means federal government is recognizing gains separately from revenue and losses separately from expenses.

Also from a definitional perspective revenue and expenses are gross inflows or outflows respectively, whereas gains or loss is a net concept. So, we believe gains and losses should be added as financial statement elements. Or for this concept statement purpose, it should be stated that expenses include losses and revenues include gains. Gain can be defined as increase in net position from peripheral, or incidental, transactions of an entity. Losses can be defined as decreases in net position arising from peripheral, or incidental, transactions of the entity.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

NASA Response: It is not clear from the paragraph what kind of intangible assets and long-term social obligations are being discussed. For example, employees of the federal government are assets of the entity, but are not recognized as such in the financial statements. The “knowledge asset” is a very valuable intangible asset in the federal government, and very structured system of knowledge management is undertaken by many entities. But again, we don’t believe that it should be treated as an additional element.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A, page 29.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

NASA Response: We agree with the proposed concept statement and disagree with the alternative approach. A liability should be recognized based on the result of past transactions or events. The transactions have already occurred, and the fact that Congress has the authority to change the law in the future should not prevent the financial statement from reflecting the current conditions.

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)

- a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

NASA Response: We agree that the concept of future economic benefit and control over the economic benefit or service are essential characteristics of a federal asset. But the future economic benefit is a probable benefit; the term probable is missing from the characteristics.

But there are current federal assets reported in the financial statements that do not meet all of the essential characteristics. Some assets such as space exploration equipment may not meet the characteristics of future economic benefit because of the unique nature of the projects under which these types of assets are manufactured and the nature of the

asset itself. The difficulty is inherent in the distinction between basic research scientific benefits and economic or financial benefits. Typically, long-term research efforts to gain knowledge may or may not produce a specific economic output, but may provide scientific benefits in the long-run. While these types of assets are being constructed and later deployed to the destination, there is a high level of uncertainty about the future economic benefit. The overarching objective of these research efforts is to gain new knowledge. As it stands now, some of these types of costs are currently treated as general PP&E even though these efforts do not meet the future economic benefit criteria. These costs should be considered as Research and Development costs and expensed instead of capitalizing the costs.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

NASA Response: We believe that an asset should embody a probable future economic benefit. This means an asset has the capability to contribute directly or indirectly to future net cash inflows. Also the transaction or event giving rise to the entity's right to or control of the benefit has already occurred.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

NASA Response: We agree that liabilities represent obligations to provide assets or services to another entity. But the future sacrifice of economic benefits arising from present obligations of a particular entity must be probable in order to be recognized. The concept of probability is not addressed in the first characteristic. We also believe that from a conceptual stand point, a liability need not be represented by a written agreement, nor be legally enforceable. For example, a federal entity might choose to pay a terminated employees salary for a period of time after termination even though not legally required to do so.

We believe strongly that the second characteristic of Liabilities needs further clarification. As proposed, this characteristic requires the existence of an identifiable other entity and an agreement or understanding as to when settlement of the obligation is to occur. Currently the estimated cost of hazardous materials contamination clean-up at Federal facilities is recognized as a liability when the cost can be reliably estimated. However, in many cases the clean-up will not occur until some time in the future and the other entity who will perform the work and receive payment has not been identified. In these cases there does not seem to be an actual "other entity" and there is no agreement or understanding with that entity concerning the settlement of the obligation the government will have to that entity. The proposed element definition should clearly state how both characteristics can be satisfied in these types of situations.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?

NASA Response: No. We believe that if the application of the second characteristic is clarified as requested in our response to question 5.a., the proposed characteristics are the fundamental essential characteristics of a liability.

6. As indicated in Question 1a), the first principle of the Board's approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

NASA Response: We believe that the definition of asset and liability should be expanded to include the concept of probability, because assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events and liabilities are probable future sacrifice of economic benefits arising from present obligations. From a financial reporting perspective, if the future economic benefit is not probable, and measurable, it cannot become a reportable element on the face of the financial statements. Also, once the test of probability is met, we determine whether the transaction is measurable for recognition purpose. For example, if the collectibility of accounts receivable is not probable, it does not meet the definition of an asset.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

NASA Response: We agree that net position is a residual amount. For revenue and expense, we suggest emphasizing the concept of gross amount because revenue and expenses are gross amount compared to gains and losses, which are net amounts. Also revenues are inflows and expenses are outflows.

With regards to gain and loss, earlier we recommended considering them as separate elements from revenue and expense because of their peripheral or incidental nature. In paragraph 56 of this document under definitions of revenue and expense, it is stated that gains and losses are considered subsets of revenues and expenses. We believe that gains and losses are distinct from revenues and expenses and should not be treated as their subsets. For example, when a piece of machinery sold for an amount greater than its book value, a gain would result. So, gains are net inflows, measured as the difference between amount received and book value. But revenues are gross inflows, measured as the amount received for goods or services without regard to the cost of providing goods or services.

7. The proposed concepts statement establishes two conditions ("recognition criteria") that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

NASA Response: We recommend adding the criteria of relevance and reliability. Relevance and reliability are two primary qualitative characteristics of accounting information. Both these elements are critical for decision usefulness. No matter how reliable, if information is not relevant to the decision at hand, it is useless. Conversely, relevant information is of little value if it cannot be relied on.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element ("existence probability"), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 25.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

NASA Response: We agree with the alternative view that the proposed concept statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element and (2) there exist a threshold where such probability is so slow that an item would not meet the definition of an element. If the existence of an asset is

assessed without considering the “existence probability”, it could result in identifying a large number of assets, which later turn out to be of no value from a reporting perspective. Theoretical and conceptual discussion about financial statement elements should be weighed and discussed with the overall objectives of federal financial reporting and other qualitative characteristics of accounting information.

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting. (See paragraphs 57-61)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views, page 26.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

NASA Response: We agree with the proposed Concept Statement definition of “measurable” and believe that there is no need to explicitly discuss an assessment of probability when deciding whether an item is measurable or to discuss threshold at which an item is not measurable. The question of measurement involves two choices: (1) the choice of a unit of measurement and (2) the choice of an attribute to be measured such as historical cost, net realizable value, present value of future cash flows etc. There are generally accepted accounting practices for calculating these amounts using the monetary units. So we don’t believe an assessment of probability is needed in this situation.

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the

characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.) (See Appendix A: Alternative Views, page 27.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

NASA Response: We concur with the Alternative View that the qualitative characteristics of financial statements should be considered while determining whether an item meets the recognition criteria.

The qualitative characteristics of reported financial information should be considered while defining the financial statement elements, otherwise a large number of items that might not meet the qualitative characteristics might be recognized. For example, the primary qualitative characteristics of relevance and reliability need to be considered for financial reporting, the secondary quality characteristics of comparability and consistency are also important from the reporting perspective. Recognition, and measurement concepts has two elements; Assumptions and Accounting Principles. Economic entity, periodicity, going concern and monetary unit are all assumptions used while defining a financial statement element. Accounting principles such as historical cost, realization, matching and full disclosure should also be considered when defining financial statement elements. We believe that not including these qualitative characteristics here would make this Concept Statement less understandable.



SOCIAL SECURITY

Office of the Chief Actuary

August 15, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
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Washington, DC 20548

Dear Ms. Comes:

I appreciate the opportunity to comment on the June 7, 2006 Federal Advisory Accounting Standards Board's Exposure Draft, Definition and Recognition of Elements of Accrual-Basis Financial Statements.

I support presenting the basic definitions of certain elements of accrual accounting in a single concept statement. Such a document has the potential to be a valuable resource to both the preparers and users of financial statements and can make such statements more consistent, understandable, and transparent. However in general, I agree with the positions taken by the alternative view in determining the best course of action for developing this statement. I also suggest that the financial reporting community would be better served if the Board retains the definitions of assets and liabilities that have been established in previous standards. These definitions provide clear guidance and are both relevant and appropriate to our office's work in providing input to the Social Security Administration's financial statement and the government-wide financial statements.

The proposed new liability definition, which contradicts the definition in SFFAS 5, would cause confusion for both producers and users of the statements. And of course such broad change would make comparisons to prior year's financial statements difficult. Of primary concern, are the removal of the probability threshold from the definitions and the directive to ignore the basic power of Congress to change the law. These changes would result in asset and liability definitions so broad that they could lead to unnecessary and excessive expansion of recognized items on the balance sheet and result in a significant reduction in the readability, relevance, and reliability of the financial statements. The enclosure contains responses to the questions listed in the exposure draft.

Given the general nature of the applicability intended for the proposed definitions for all federal government financial reporting, it may be premature to focus singularly on social insurance. But it is difficult to avoid that focus given the size of the obligations that potentially could be recognized in comparison with liabilities recognized for the rest of the federal government. Specifically, the nature of social insurance obligations is such that the FASAB has long recognized that only benefits that are both due and payable represent liabilities of the federal

government. This recognition is entirely consistent with the nature of the financing of and the obligation to provide the scheduled benefits and renders the financial statement an entirely relevant and appropriate indicator of the government's current financial position. Any loosening or expansion of the definitions that would expand what might be recognized as a liability under these social insurance programs would ill serve the public, the news media, legislators, program managers, and other users of this information. Emphasis on such expanded concepts would misinform and lead to inappropriate conclusions about the financial status and sustainability of these programs. Specifically, a program that had been well conceived and maintained an ability to meet obligations on a pay-as-you-go basis could none the less end up with a substantial unfunded obligation under an expanded definition of liability. In this case an entirely inappropriate message would be conveyed to users of the statement.

Thank you in advance for taking my comments into consideration, I truly appreciate the work the Board has done over the past 15 years in providing standards and guidance in preparing financial statements that faithfully represent the government's financial position. I hope to continue working with the Board on the further development of this concept statement and other projects that will add value to federal financial reporting.

Sincerely,



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Enclosure

cc:

Jo Anne B. Barnhart
Linda Combs
Don Hammond
David Walker
Donald Marron
Dale Sopper

Responses to Questions listed in the FASAB Exposure Draft
Definition and Recognition and Measurement of Elements of Accrual Basis
Financial Statements
From Chief Actuary, Social Security Administration August 15, 2006

Question 1(a):

Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Answer: Yes, definitions of assets and liabilities derive from their fundamental or essential characteristics. This seems clear in general. But this simply means that care must be taken in determining the characteristics, and in recognizing that what is essential and fundamental in one context may not be fundamental and essential in all contexts.

Question 1(b):

Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Answer: Yes, definitions of net position, revenues, and expenses should generally derive from the definitions of assets and liabilities. This again means that care must be taken in determining the characteristics, and in recognizing that interrelationships among these elements may vary to a degree depending on the nature of the program, its obligations for expenditures, and its basis for financing.

Question 1(c):

If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Answer: Yes, an item that meets the definition of an asset is an asset even if it is assessed to be too small to be material. However, if a potential *asset* is not measurable in the sense that it cannot be quantified in monetary terms, it is questionable whether it should be considered an asset in a financial sense. Should such non-quantifiable assets be included in financial statements then the fundamental difference between them and quantifiable financial assets should be described. This is precisely an example of the necessity for some flexibility in assigning fundamental and essential characteristics of assets and liabilities.

Question 2(a):

Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Answer: I agree with the FASAB alternative view that additional elements, beyond the five identified within the proposed concept statement, need to be explored. The proposed statement defines elements traditionally associated with financial accounting for the private sector and develops analogous definitions for those elements within the context of the federal government. This approach leaves a possibly incomplete listing of elements and thus may not reflect the true nature of the federal government's financial position or activities. Some potential obligations, for example, may not meet the characteristics of a liability for any number of reasons, but might none the less be of sufficient significance to be mentioned, but not as a liability. For such cases an additional element might be defined. Such an element would not represent a liability, and should at most be recognized as supplementary information provided within the overall financial statement.

SFFAC 1 correctly notes that "The federal government is unique in that it has continuing responsibility for the nation's common defense and general welfare". Carrying out these unique responsibilities causes the government to have unique resources and scheduled financial outlays that have no private counterpart. The elements used in the federal financial statements could incorporate items such as the government's intangible resources and scheduled social insurance benefits using definitions that represent their true substance rather than forcing them into the more limited definitions of assets and liabilities presented in the proposed statement for inclusion on the balance sheet.

The Board has recognized the government's unique status previously by developing new financial statements and exploring additional avenues to present the federal government's financial position. For example, the Board recently made the Statement of Social Insurance (SOSI) a basic financial statement with the same level of importance and held to the same auditing standard as the income statement and balance sheet. No such financial statement is used in the private sector as these government programs are very different in nature from any corporate endeavor and thus the accounting treatment is rightfully different.

Question 2(b):

Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Answer: The scheduled Social Security revenue and benefits presented in the SOSI are very different from the basic elements that have been developed in the proposed statement. Paragraph 2 states that the five elements will comprise the building blocks of financial statements. This seems to contradict the fact that the information presented in the SOSI, which

beginning this year is a basic component of the financial statement, is not necessarily comprised of these five elements.

In addition, I am aware that the Board is planning on developing a taskforce to determine the definition, measurement, and display of federal financial sustainability. Since it is likely that these scheduled outlays and revenues will play a vital role in the sustainability project, perhaps the taskforce should also be directed to identify their essential characteristics. Rather than delaying the issuance of this standard, we suggest simply adding wording indicating that this list is not exhaustive and that other elements exist and providing scheduled social insurance benefits as an example of something that does not fall into one of these categories.

Question 3(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Answer: I agree with the alternative view that the government's power to modify the law at any time and in any way affects the existence of a present obligation. The exposure draft states "the federal government is governed by and operates in a framework of laws". The primary document that provides that framework, the U.S. Constitution, gives Congress the power to change existing law. It is often said that one Congress cannot bind another. To state that present law should be considered but ignore the fact that the law can be changed at will is contradictory.

Question 4(a):

Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Answer: I agree that embodying economic benefits or services for the future and the ability to control access are essential characteristics of federal government assets.

Question 4(b):

Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government assets?

Answer: No, I do not believe there are additional essential characteristics that apply to all federal government assets.

Question 5(a):

Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an

example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

Answer: I agree that existence of a present obligation to provide assets and an understanding of settlement are essential characteristics of a federal government liability. But I have two concerns. First, these are not the only characteristics common to federal government liabilities (see 5(b)) and second, the definition of present obligation and understanding are critical. Thus, more is needed and these two characteristics need to be drawn appropriately.

As previously stated, we believe that the Board should continue with the definition of a liability, issued in SFFAS 5, as “A liability for federal accounting purposes is a probable future outflow or other sacrifice of resources as a result of past transactions or events.” This definition basically allows for two essential characteristics that cover all federal liabilities: 1) it is a probable future outflow and 2) the outflow is a result of a past transaction or event.

The proposed characteristics make no mention of probability. This could allow for a large expansion of the liabilities to be recognized for improbable events. Then when the outflows do not occur they would be removed, most like to be replaced by additional liabilities for improbable events. This has the potential to result in financial statements that are inconsistent. Paragraph 57 of the proposed statement states that “Uncertainty about economic activities and results is pervasive and often clouds whether a particular item qualifies as an asset or liability as the definitions are applied”. Since probability and uncertainty are so pervasive in applying the definitions, it would be helpful if the definitions themselves explicitly mentioned that probability should be taken into account.

In addition it would be helpful if the Board expands on the types of events or transactions stated in paragraph 41 that can result in a liability. I recommend that the board tie these into the past events and transactions presented in paragraph 19 of SFFAS 5. Those classes include (1) past exchange transactions, (2) government-related events, 3) government-acknowledged events or (4) non exchange transactions that according to current law and applicable policy are unpaid amounts due as of the reporting date. These classifications identify the different classifications of federal activities and how they differ in substance from what is presented in other entities’ financial statements.

Question 5(b):

Are there any *additional* characteristics that are *fundamental* or *essential* to *all* federal government liabilities?

Answer: Yes, it seems important to have symmetry between the definitions of liability and asset. In the fundamental concepts outlined for a federal government asset, the second essential characteristic stipulates that the asset must be an economic benefit that cannot be controlled, altered, or diminished at will by another entity. This fundamental characteristic of an asset should also apply to a liability. The additional characteristic of a federal government liability should stipulate that the liability cannot be controlled, altered, or diminished at will by the

federal government. To fail to include this characteristic for a liability would create an inconsistency that should obviously be avoided.

Question 6(a):

Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

Answer: We agree that the definitions of assets and liabilities should be derived from their essential characteristics. As noted in 5(b) above, however, a fundamental characteristic of a federal government liability is missing, that the federal government not have the ability to alter the liability at will. This characteristic is related to discussion of the laws governing Federal financial transactions.

As presented in the exposure draft, the definition of a liability seems to be derived not just from the essential characteristics, but also by the legal framework section in paragraphs 35-37. The legal framework states “a federal liability must have its foundation in law”, thereby creating an additional characteristic that all liabilities share.

Also in paragraphs 35-37, characteristics are given that some liabilities may have but that others do not. For example, legal enforceability, contractual arrangements, and liabilities directly flowing from law are discussed prior to defining a liability or its essential characteristics. This could be confusing and takes away from the Board’s goal of deriving the definition solely from the element’s essential characteristics.

In addition, no such legal framework was identified in the asset section and its placement in the liability section is unnecessary as all of the government’s actions and resulting liabilities and assets have their foundation in law. In order to eliminate any potential confusion and keeping with Board’s desire that the definitions be derived solely from the essential characteristics, I suggest that the Board remove paragraphs 35-37 and leave these issues to be addressed in individual standards.

Question 6(b):

Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

Answer: With the caveat noted above about the definition of federal government liabilities, the definitions of net position, revenues, and expenses seem to adequately convey the relationships to assets and liabilities.

Question 7(a):

Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

Answer: No, meeting the definition of an element and being measurable seem adequate. However, the definitions should include consideration of probability and, in the case of liabilities, ability to alter the liability, as noted above.

Question 8(a)

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

Answer: I agree with the alternative view and the view the Board presented in SFFAS 5 and feel that probability should be explicitly taken into account both in applying the elemental definitions and measurement. Again, removal of the probability thresholds could result in improbable and therefore immaterial and irrelevant items being recorded on the balance sheet. Recording improbable events on the balance sheet could compromise the relevance of the financial statements, as users expect the statements to accurately capture the true substance of the federal governments' past transactions and events.

Question 9(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

Answer: I concur entirely with the alternative view. Assessment of the probability of an event is essential in determining whether it meets the threshold of materiality and is meaningfully measurable. Omitting the consideration of probability would lead to the inclusion of confusing and irrelevant items that would obscure the true net position of the entity.

Question 10(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

Answer: I agree with the alternative view that the statement should explicitly acknowledge that all of the qualitative characteristics of financial reporting, specified in SFFAC 1, be taken into account

While I suggested in my response to question 6 that the legal framework section be removed, there is one comment in paragraph 36, “some liabilities are construed from the totality of the conditions and factors for a particular situation”, that I think is very important. This statement should be expanded to conclude that all liabilities and assets are determined by the totality of their respective facts and circumstances. Specifically referencing the qualitative characteristics of SFFAC 1 seems to be the easiest way to do this and would maintain consistency between the concept statements.

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Overall Comment

We have reviewed the Concepts Statement on the Elements of Accrual-basis Financial Statements ED and are in agreement with the new conceptual framework for first identifying assets and liabilities then proceeding through the measurement and recognition process.

Environmental Liabilities

Federal Financial Accounting and Auditing Technical Release No. 2 requiring a legal liability does not appear to be consistent with section 36 of the ED. Technical Release No. 2 states that an agency is responsible for recognizing government-related environmental clean-up costs resulting from past transactions or events when a future outflow or other sacrifice of resources is probable and can be reasonably estimated. A key factor for determining whether a future outflow of resources is probable is whether the contamination is government related and the agency is **legally liable** [emphasis added]. However, it appears that the FASAB may not have anticipated a situation whereby a Federal agency has a Treaty obligation to remediate environmental incidents, but does not have the requisite **legal liability** [emphasis added] because the treaty document does not have a liability protocol. We believe, consistent with section 36 of the ED, that the intent of the standard is to record a liability when an agency has a legal liability or obligation, responsibility, and requirement to remediate environmental liabilities. However, in this instance, the technical release appears to preclude Federal agencies from doing so. Therefore, the FASAB should clarify the Federal government's responsibilities for environmental clean-up costs when it has an obligation, responsibility, and requirement to remediate environmental liabilities but does not have a legal liability to do so to ensure consistency with the ED.

Federally Funded Research and Development Centers (FFRDC)

The Federal Government including NSF funds many FFRDCs. NSF engages FFRDCs in cooperative agreements and contracts to manage, operate and maintain research facilities for the benefit of the scientific community. As part of these agreements and contracts, NSF funds on a pay-as-you-go basis certain employee benefit costs, (accrued vacation and other employee related liabilities, severance pay and medical insurance), long term leases and vessel usage. In addition, these agreements permit certain FFRDCs to make claims for any unpaid costs upon termination or non-renewal of the agreements and contracts. However, one FFRDC operator has identified termination payments as obligations of NSF, rather than recording these liabilities on its own financial statements. NSF, as the funding agency, may ultimately be potentially liable because the activities of its FFRDCs are wholly supported by NSF funds. Therefore, we believe that FASAB should clarify the Federal government's treatment of assets and liabilities of FFRDCs to ensure the consistent treatment of these assets and liabilities government-wide.

Federal Accounting Standards Advisory Board Exposure Draft - Definition and Recognition of Elements of Accrual-Basis Financial Statements

We appreciate the opportunity to review and comment on the FASAB Exposure Draft, Definition and Recognition of Elements of Accrual-Basis Financial Statements, dated June 7, 2006. The Department of Health and Human Services, Office of Inspector General comments follow:

1a). Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Yes, the definitions of assets and liabilities should be derived from their fundamental or essential characteristics. However, we believe the definitions for these elements should be similar to the definitions contained in the Financial Accounting Standards Board's (FASB) Concept 6, *Elements of Financial Statements*. Currently, the definitions in SSFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19) are very similar to those in FASB Concept 6.

We believe the current proposed definitions do not encompass all of the characteristics or unique features of the elements. For example, SFFAS 1 notes that FBWT is an asset because it represents the entity's claim to Federal government resources. Therefore, the current proposed definition would need to be expanded to include a claim to a resource. Given the recognition criteria established includes meeting the definition of an element, we believe the definition should contain the essential characteristics. For example, paragraph 33 of the exposure draft notes that implicit in the definition of assets is that the event giving rise to the government's ability to control access...must have occurred. We do not agree that this is inherent and believe that the definition should specifically state, "as a result of past transactions or events."

Overall, we believe the proposed definitions should be changed to reflect to be more consistent with definitions already contained in current FASAB Statements, as well as definitions in FASB Concept 6. For example,

- Assets are probable future economic benefits obtained or controlled by a Federal Government Entity as a result of past transactions or events.
- Liabilities are probable future outflows or sacrifices of resources arising from present obligations of a Federal Government Entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.

1b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Yes, the definitions of net position, revenues, and expenses should be derived from their fundamental or essential characteristics. However, we believe the definitions for these elements should be similar to the definitions contained in the Financial Accounting Standards Board's (FASB) Concept 6, *Elements of Financial Statements*. Currently, the definitions in SSFAS No. 6 (Appendix E Glossary) are very similar to those in FASB Concept 6. For example, SSFAS 6 defines expense as, "Outflows or other using up of assets or incurrences of liabilities (or a combination of both) during a period from providing goods, rendering services, or carrying out other activities related to an entity's programs and missions, the benefits from which do not extend beyond the present operating period. (Adapted from Kohler's Dictionary and FASB Concepts Statement No. 6)."

1c). If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

Yes, we believe if an item meets the definition of an asset it is an asset. Generally, if an item meets the definition and is measurable, it should be reported in the financial statements. If an asset meets the definition but is not measurable, it should be disclosed in the accompanying footnotes.

We believe the statement regarding materiality should be clarified, see comment 7a below. An item may individually be immaterial however a number of individual immaterial items may be material in aggregate.

2a). Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Yes, since we believe the element definitions should be similar to FASB Concept 6 we believe that gains and losses should be defined in the Concepts Statement. In addition, this supports information in current FASAB statements. For example SSFAS 7, distinguishes between when a gain or loss should be recognized rather than revenue or expense.

2b). Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

See comment 2a.

3a). Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability

to change laws on the recognition of a liability? Please explain the reasons for your position.

We support the position taken in the proposed Concepts Statements. This is consistent with current text in the SSFAS No. 5.

4a). Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

See comment 1a. We believe the implicit characteristic under the second essential characteristic should be broken out separately, that is “the transaction or other event giving rise to the entity's right to or control of the benefit has already occurred.” Generally, however the characteristics appear similar to those identified in FASB Concept 6.

4b). Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government assets?

See comment 4a.

5a). Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

See comment 1a. We believe the second essential characteristic, “...the government and the other entity involved have an agreement or understanding concerning the settlement” is too vague. We believe the characteristic should support the current definition in SSFAS 5; that is, “as a result of past transactions or events.” As FASB Concept 6 states, “Only present obligations are liabilities under the definition, and they are liabilities of a particular entity as a result of the occurrence of transactions or other events or circumstances affecting the entity.” The current proposed characteristic does not distinguish the difference between present and future obligations of an entity.

5b). Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities?

See comment 5a.

6a). Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

See comment 1a.

6b). Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

See comment 1b.

7a). Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

We recommend the wording in paragraph 8 regarding the influence of assessments of the materiality be clarified to ensure that items that have been measured but are considered immaterial are not excluded from the financial statements. Consistent with FASB Concept 6, “To be included in a particular set of financial statements, an item must not only qualify under the definition of an element but also must meet criteria for recognition and have a relevant attribute that is capable of reasonably reliable measurement or estimate. Thus, some items that meet the definitions may have to be excluded from formal incorporation in financial statements because of recognition or measurement considerations.”

We believe the qualitative characteristics should be considered as part of determining whether an item meets the recognition criteria. Consistent with FASB Concept 2, Qualitative Characteristics of Accounting Information, emphasizes that usefulness of financial reporting information for those decisions rests on the cornerstones of relevance and reliability.

8a). Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

We agree with the current approach taken and it is implicit in the proposed Concepts Statement.

9a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

We agree with the current approach taken and it is implicit in the proposed Concepts Statement.

10a). Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the

qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

See comment 7a.

August 11, 2006

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Subject: Exposure Draft: *Definition and Recognition of Elements of Accrual-Basis Financial Statements*

Dear Ms. Comes:

This letter provides comments from the Bureau of Economic Analysis (BEA), the nation's national accountant, on the subject exposure draft (ED). Our comments have two purposes: (1) They are intended to highlight the need for convergence in international accounting standards; and (2) they request modifications to the proposed standard that will increase its usefulness. We request that these comments be considered, even though they are being submitted after the comment period's closing date.

Comments

Convergence of international accounting standards

For the past three years, BEA has participated in an effort to revise the *System of National Accounts, 1993 (SNA)*. That effort included collaborations with other nations and with organizations that are responsible for developing and promulgating international accounting standards. Among the latter, the International Public Sector Accounting Standards (IPSAS) Board, provided significant input into the *SNA* revision process, and forced the recognition of the importance of convergence of government accounting standards across nations. In BEA's view, the estimates that we prepare for our worldwide data users are useful only to the extent that our source data and methods are harmonized with those of other nations. We recognize that our source data will become more consistent with those of other nations when the accounting standards that are used to produce those data are consistent with international standards. Therefore, BEA urges the Federal Accounting Standards Advisory Board (FASAB) to consider the IPSAS, and to seek convergence with it, when finalizing the proposed standard.

Requested modifications

BEA requests the following two modifications to the proposed standard:

Consider modifying the proposed standard to identify, define, and highlight an additional important factor of accrual-basis financial statements: "Transactions." While assets, liabilities, net position, revenues, and expenses are essential elements of financial statements, transactions constitute the antecedent events that facilitate the formation of the aforementioned elements. In fact, the nature of transactions often signals the types of elements that are to be recorded in financial statements. Transactions are not normally identified in the body of financial statements; however, they are often described in the footnotes to financial statements. Although definitional and conceptual statements on transactions do not appear in all international accounting standards, the *SNA* provides extensive definitional and conceptual statements on transactions in the context of national economic accounting (see §3.12 - §3.56).¹ Therefore, as the underlying basis for the elements in financial statements, BEA requests that FASAB provide definitional and conceptual statements on transactions in the proposed standard. In addition, please state in the proposed standard that transactions are an important underlying factor for the five elements that are presented in financial statements.

To the extent that FASAB has existing conceptual and definitional statements on transactions that are reflected in an existing standard, then it would be sufficient to reference that standard in the proposed standard.

- In reference to Part 4 of the ED and the characteristics that are fundamental or essential to all federal government assets, it is true that an asset can embody economic benefits or services that can be used in the future. However, it is also true that assets may rise or fall in value. For example, the value of fixed assets may be driven to zero by depreciation, catastrophes, or obsolescence; that is, they may lose an essential characteristic of assets. It is worth mentioning that the *SNA* refers to increases in the value of assets in its basic definition of assets (see §13.12). Therefore, BEA requests that FASAB consider expanding the currently listed characteristics of assets that appear in the ED to include the characteristic that assets may increase or decrease in value and may, thereby, become devoid of a characteristic that is fundamental to assets.

BEA thanks FASAB for the opportunity to comment on this ED, and hope that our comments will increase the usefulness of the proposed standard as a tool for preparing financial statements.

Please contact us if you have questions.

Sincerely,



Brooks B. Robinson
Chief, Government Division

CC: Brent R. Moulton, Associate Director for National Economic Accounts

¹ Our review of General Accepted Accounting Principles (for balance sheets and income statements) and of International Public Sector Accounting Standards did not unearth extensive definitional or conceptual statements on "transactions."



CFOC (some letters submitted separately are repeated here) - Preparer

United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, DC 20240



AUG 16 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Enclosed is the Chief Financial Officers Council – Standardization Committee's FASAB Response Work Group consolidated the responses from the Council members on the subject Exposure Draft.

If you have any individual concerns that need my personal attention do not hesitate to contact me at 202-208-5225.

Sincerely,

Daniel L. Fletcher

Director

Office of Financial Management

Enclosure

Question 1(a):

Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Response 1(a):

Yes, the definitions of assets and liabilities should derive from their fundamental or essential characteristics. Ignoring the fundamental nature of assets and liabilities may result in definitions that are arbitrary and subject to interpretation. By defining assets and liabilities according to characteristics, agencies are given more specific guidance to help identify assets and liabilities in order to prepare financial statements in accordance with OMB Circular A-136 "Financial Reporting Requirements." Definition and recognition are not as easily segregated for financial statements of governments and the validity and usefulness to readers must be weighed to avoid burdening the readers with too much information.

Question 1(b):

Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses.

Response 1(b):

Yes, the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. The inflows and outflows of an entity are a direct result of the management of the assets and liabilities as they relate to the production of goods or services of the entity.

Net Position: The proposed definition (in short, difference between total assets and total liabilities) is acceptable. Some members believe, however, that the definition should be expanded as stated in our answer to question 6 (b). The expanded information (elaborating on the two primary components of Net Position – Unexpended Appropriations, and Cumulative Results of Operations) is important, common to all or most federal entities, and is currently included in SFFAC No. 2, paragraph 84.

Revenues and expenses result from changes in assets and liabilities and net position is equal to total assets less total liabilities. Therefore, deriving net position, revenues, and expenses from assets and liabilities is logical from an accounting standpoint. Additional clarification is requested for the recognition of imputed costs because under the entity concept (paragraph 12), some members could interpret to mean only the component-level

agency will recognize the liability and expense. This deviates substantially from previous FASAB standards that require cost recognition without matching liabilities to achieve full-cost accounting. This issue is also discussed in response 6(b).

Expenses: Some members believe this definition is unclear, and have recommended revised wording in the answer to question 6 c).

Question 1 (c):

If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reason for your position.

Response 1(c):

Yes, if an item meets the definition of an asset it should be considered an asset even though it would not be recognized on the financial statements. The proposed Concepts Statement states that "An asset that is not recognized in the body of the financial statements would be a CANDIDATE for disclosure in the notes," but this statement does not question the validity of the element. It is important to other financial and management controls to identify assets regardless of its financial statement treatment.

Currently, agencies are required to reference a note on the balance sheet that discloses information about heritage assets and stewardship land, but no asset dollar amount should be shown. The note disclosure provides minimum reporting requirements, including a description of major categories, physical unit information for the end of the reporting period, physical units added and withdrawn during the year, a description of the methods of acquisition and withdrawal, and condition information. Generally, valuation is difficult if not impossible but presentation and disclosure have been required.

In addition, an item can also be an asset and not disclosed in the financial statement or footnotes, if it can't be measured or is immaterial. Reporting these items would be excessive to preparers of financial statements and would result in less relevant information for readers of the financial statements. For example, property or equipment not meeting minimum capitalization threshold or useful life requirements should be expensed rather than capitalized. Expensing items below the threshold does not change the characteristics of the resource but allows preparers to weigh the cost of tracking the details of those items against the benefits of matching that utility to future periods in a precise manner. Therefore the members agree that definition and recognition are separate concepts that must be clearly defined.

Question 2(a):

Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Response 2(a):

Recognizing that FASAB has a project related to social insurance and the applicability of liability definitions, there should be an expectation that additional elements may be contained there. Perhaps this Concepts Statement should refer to these other projects and possibly recognize the inherent complexities of Federal accounting such as exchange, non-exchange, government-acknowledged and government-related.

Some members believe that, consistent with FASAB standards (SFFAS No. 7 and SFFAS No. 21), there could be two additional elements of accrual-basis financial statements for Federal entities – a) Other Financing Sources (the word other is used in SFFAS No. 7 to distinguish this from revenues); and b) Prior Period Adjustments. Both of these categories are different in important ways from the five proposed elements. The members believe it is of significant benefit to readers of Federal financial statements to continue to treat Other Financing Sources and Prior Period Adjustments as distinct categories. For example, Appropriations Used, and Imputed Financing, is unique and substantially different than traditional revenue reported on a financial statement.

In addition, some members would like consideration to be given to the unique treatment of gains and losses that may be required in a government entity even though they are tied to revenues and expenses in presentation.

Question 2(b):

Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

Response 2(b):

Although most items can be categorized as an asset or a liability, the nature of some items do not fit the stringent definitions of either. The nature of social insurance obligations is different than a traditional liability. Future scheduled social insurance payments may not be present obligations of the federal government and they may not be contractual commitments of the federal government. Benefits for individuals do not represent exchange transactions because they are not directly tied to taxes they have paid. Consequently, benefit entitlements are non-exchange transactions. We believe that the

FASAB should consider additional elements to provide a basis for further reporting requirements related to commitments and resources that do not meet the definitions of assets and liabilities. Furthermore, we are proposing additions to the definitions of assets and liabilities or their presentation in order to be more inclusive and more informative than when presented on the face of existing financial statements.

Question 3(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

Response 3(a):

Due to the fact that the federal government has the right to alter scheduled benefits in any manner at any time, some members support the alternative view that the government's power to change laws affects the existence of a present obligation. However, some members do believe that the presentation of obligations should be based upon information known at the time of preparation and not effected by possible changes in law. All members have not been given the opportunity to judge the possibility of alternative approaches to the presentation of these unusual elements and we hope this project can include those possibilities.

Some members have stated an entity's balance sheet provides a snap shot of its financial position at a specific point in time. In order to provide open and full disclosure and accurately present the financial position of an entity at that given point in time, financial statements must be based on present laws, regulations, and generally accepted accounting principles regardless of whether or not that position may change in the future. Providing this full and open disclosure allows stakeholders to respond in a manner that could improve the future financial position of the entity (i.e. force change in current laws and regulations that may increase assets or reduce obligations of the Federal government).

Question 4(a):

Do you agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

Response 4(a):

Yes, we agree that there are two characteristics that are essential characteristics of all federal government assets; (1) it is a resource that embodies economic benefits or services; and (2) the federal government can control it. It is very important that the federal government can control the asset. An agency may have title to an asset but not control it and if that is the case, the asset should not be recognized on the entity's balance sheet. In the ED, proposed concept example under paragraph 30 should be removed as it is confusing. It raises more questions than it answers and does not follow the exception back to the guidance. It may be more appropriate to do an example of the general rule versus the exception.

Some members contend that the two proposed essential characteristics of assets do not fully encompass all types of assets. For example, accounts receivable and loans receivable represent a claim to future resources and benefits. However, there is no time-frame specified in the asset characteristics as there is in the definition of a liability and many assets embody future and not current economic benefits. The discussion of the capitalization of leases is too broad and may result in agencies capitalizing large dollars in operating lease expenses as capital leases. Clarification is needed in accounting for lessor/lessee activity. The language stating that the party who manages and utilizes the asset should record the asset (paragraph 13) is not consistent with current accounting standards. The use of asset control as a determining factor for lease capitalization creates ambiguity and will require further guidance.

Question 4(b):

Are there any additional characteristics that are fundamental or essential to all federal government assets?

Response 4(b):

No, there are no additional characteristics that are fundamental or essential to all federal government assets. Although we do not believe there are fundamental or essential characteristics affecting all assets some receivables clearly encompass a need to recognize a probable future economic benefit such as accounts receivable, notes receivable and capital leases.

Question 5(a):

Do you agree with the proposed Concepts Statement that there are two characteristics that are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or

commitment that you believe is a liability but does not possess one or both of these characteristics.

Response 5(a):

We agree with the alternative view that the probability of existence of a liability, as in the case of contingencies, should be a component of the definition of a liability as presented in this Concepts Statement. By ignoring probability of existence, the federal government will have to accrue a contingent liability for which it disputes regardless of the probability of a negative outcome. Further, the language that states that a liability can only exist if two or more entities are involved does not take into account situations where an agency may have a liability to itself as is the case with environmental cleanup liabilities. The entity concept is not well defined. These new guidelines will remove the need to accrue liabilities for "government-acknowledged events" because the circumstances giving rise to these events generally do not involve a second entity or a specified date. While the Concept Statement will reduce the need to recognize certain liabilities that are currently recognized, the proposed definition of a liability is more closely aligned with that preferred by legal council.

While we recognize the intent of the proposed concept paragraph 36 for all federal government liabilities, we feel this definition actually increases the grayness of the definition rather than providing clarity to it since the paragraph will only increase the level of debate more than it is currently between a legal liability and accounting liability. Therefore, we feel that the proposed concept under paragraph 36 should be removed.

Dramatic Expansion of the Definition of Liability:

The last sentence of Exposure Draft, paragraph No. 41 states the following, "A present obligation is incurred when the government takes a specific action that commits or binds the government and affects another entity."

This sentence dramatically expands the definition of a liability, and could include undelivered orders (i.e. purchase orders, contracts, memorandum of agreement/understanding) and possibly commitments where goods or services have not yet been received or the underlying event has not taken place. This definition of a liability is entirely inconsistent with traditional accrual-basis accounting for liabilities including accrual-basis accounting for liabilities as currently defined by FASAB in SFFAC No. 2, paragraph 84 and SFFAS 5, paragraph 19, and as defined by the Financial Accounting Standards Board (FASB), and as defined by the Governmental Accounting Standards Board (GASB). An undelivered order or commitment, while being a commitment of the government, should not be a liability (amount owed) of the government because the providing entity has not yet met its commitment or the underlying event has not yet taken place. The existence of a Federal liability is

contingent upon the providing entity adequately providing the goods/services or the underlying event taking place. Until the providing entity adequately provides the goods/services or the underlying event takes place, the Federal Government is not liable to pay for those goods/services.

Some members are very concerned about this dramatic expansion of a liability, because they believe that (consistent with private sector and state/local practice) readers of financial statements expect liabilities to be amounts owed by the government for goods/services received or underlying events that have taken place. To have liabilities include, for example, undelivered orders and possibly commitments, may cause liabilities as reported on the Balance Sheet to not be meaningful or useful to readers.

In layman's terms, some members believe that most readers of financial statements understand "liability" to be an amount "owed," and, an undelivered order, would not generally be considered an amount "owed," as the exchange of value in exchange for a promise of future payment has not yet taken place.

The federal government's definition of a liability would not be consistent with the private sector and state/local accounting for liabilities.

The reason or benefit of this significant departure from established practices across the spectrum for accrual-basis accounting has not been explained or justified by FASAB in the Exposure Draft.

"Present Obligation" Definition Should Include "Probable:"

Some members believe that the "present obligation" is an essential characteristic that needs to be "probable," for consistency with SFFAS 5, paragraph 19 (see below) and FASB accrual-basis accounting for liabilities.

SFFAS 5, paragraph 19: "A liability for federal accounting purposes is a probable future outflow or other sacrifice of resources as a result of past transactions or events. General purpose federal financial reports should recognize *probable* and measurable future outflows or other sacrifices of resources arising from (1) past exchange transactions, (2) government-related events, (3) government-acknowledged events, or (4) non-exchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date."

FASB: "Probable future sacrifices of economic benefits arising from present obligation of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions and events."

This dramatic expansion of the definition of “liability” may cause the liability recognition of many new items that do not reach the definition of “probable” and may threaten important qualitative characteristics of reporting such as relevance, reliability, cost versus benefit, and representational faithfulness.

If “probable” is omitted from the definition of a liability, the federal government’s definition of a liability would not be consistent with the current FASB definition and would not appear to be consistent with the proposed GASB definition clause “with little or no discretion to avoid.”

The reason or benefit of this significant departure from established has not been explained or justified by FASAB in the Exposure Draft.

“Settlement” Essential Characteristic

Some members believe that “settlement” is not an essential characteristic of a liability. If there is no agreement on when a liability will be paid, the liability still exists (i.e. the amount is still owed regardless of whether agreement or settlement has been reached or not).

With regard to a situation when the government is free to decide whether to settle the obligation, members agree with SFFAC No. 2, which states “...Also, because the Federal Government is a sovereign entity, it can abrogate at any time many of its liabilities arising from other than contracts. This does not, however, eliminate the existence of, and therefore the need to report, liabilities incurred by the reporting entity.” These members believe that a liability should be recorded based on current conditions and current law.

Question 5(b):

Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

Response 5(b):

No, there are no additional characteristics that are fundamental or essential to all federal government liabilities but further clarification may be needed such as “probable future outlay of resources as a result of past actions or laws.”

Question 6(a):

Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? If not, how would you modify the definitions?

Response to 6(a):

Members believe that the definition for liabilities in SFFAS 5 is superior to the definition shown in the Exposure Draft, and that the definition of Liability in the Exposure Draft is a dramatic expansion of the definition of a Liability that has not been adequately explained or addressed (please also see answer to question 5).

We agree with the Alternative View that the removal of the term "probable" greatly impacts the definitions of assets and liabilities and opens the door for immaterial and other unusual items to be recognized in the financial statements.

Question 6(b):

Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definitions?

Response 6 (b):

The new definitions of revenues, expenses, and net position imply that imputed costs will no longer be recognized because the underlying liability is not at an agency-component level. According to the guidelines stated in the entity concept (paragraph 12), imputed costs such as pension and post-retirement benefit liabilities will be incurred by the Office of Personnel Management (OPM) rather than the individual agencies. Some members believe this definition is inconsistent with FASAB SFFAS 4 which requires agencies to record imputed costs as part of recognizing the full cost of the entity.

Net Position Definition:

No. The definition for net position described in SFFAC No.2 paragraph No.84 includes a more precise definition which elaborates on the primary components of Unexpended Appropriations and Current Results of Operations as follows: "Net position is the residual difference between assets and liabilities. It is generally composed of unexpended appropriations and the cumulative results of operations. Included in the former would be appropriations not yet obligated or expended, including undelivered orders. Included in the latter would be the amounts accumulated over the years by the entity from its financing sources less its expenses and losses, which would include donated capital and transfers in the net investment of the Government in the reporting entity's assets; and an amount representing the entity's liabilities for such things as accrued leave, credit reform subsidies, and actuarial liabilities not covered by available budgetary resources."

Revenue Definition:

Members generally agree with the Exposure Draft definition of Revenue.

Expense Definition:

Some members believe that the definition of expense is very unclear, and respectfully recommends the following rewording: "An expense is a decrease in assets, an increase in liabilities, the consuming or adjusting of assets, or a combination of the above from the receipt of goods or services or any other activities during the reporting period."

Question 7(a):

Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

Response 7(a):

None other than the current conditions, in order for an item to be recognized in the financial statements, an assessment of both the probability of existence and the probability of measurement should be made. We concur with the Alternative View that the qualitative characteristics of financial reporting should be considered when determining whether or not an element should be recognized. Probability of existence and probability of measurement both have a direct impact on the reliability of the financial reports.

Question 8(a):

Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

Response to 8(a):

We concur with the Alternative View that there needs to be an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element. Some items are improbable and should not be required to be disclosed in the body of the financial statements or the footnotes.

#37 an assessment of probability threshold when determining whether an item is measurable. C-OC (some letters submitted separately are repeated here) - Preparer
If the item does not meet the probability threshold then it is unreliable; and therefore, is also irrelevant regardless of whether or not it is measurable.

of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position?

Response 10(a):

We concur with the Alternative View concerning the need for consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. By making probability of both existence and measurability part of the recognition criteria, the integrity of the financial statements will be enhanced because of the direct impact of probability on certain qualitative characteristics of financial reporting such as reliability.



CFOC (some letters submitted separately are repeated here) - Preparer
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AUG 23 2006

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RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Enclosed is the Chief Financial Officers Council letters related to concerns with the subject Exposure Draft. Twenty (20) member letters are included as enclosures, one (1) member supports this position and responded directly, two (2) members did not respond to our requests and three (3) members dissented that also responded directly. Thank you for the opportunity to respond and the extension of time you allowed for us to get these letters together.

If you have any individual concerns that need my personal attention do not hesitate to contact me at 202-208-5225.

Sincerely,

Daniel L. Fletcher
Director
Office of Financial Management

Enclosures



U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

CFOC (some letters submitted separately are repeated here) - Preparer

AUG - 4 2006

**Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548**

**RE: FASAB Exposure Draft, Definition and Recognition and
Measurement of Elements of Accrual-Basis Financial Statements, dated
June 7, 2006**

Dear Ms. Comes:

**Thank you for the opportunity to review and comment on the FASAB
Exposure Draft (ED), Definition and Recognition and Measurement of
Elements of Accrual-Basis Financial Statements, dated June 7, 2006.**

**I strongly support maintaining the current asset and liability
definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5
(Paragraph 19), respectively. The current definitions have served us
well in explicitly determining whether an item is an asset or liability for
inclusion in our agency's accrual-basis financial statements. To this
end, I support the Alternative View in Appendix A of the proposed ED.
The only exception noted was found in A10 concerning present
obligations. We noted that the ability of Congress to redefine future
obligations is not measurable with any degree of accuracy. In the
observance of the principle of conservatism, I express a dissenting
opinion of the concept that changes in law "may provide additional
evidence about whether a present obligation exists". We note that
evidence "unless founded" in quantifiable measurable terms should not
be considered present obligations. This view supports the explicit
requirement, as embodied in the current definitions, for an assessment
of existence probability and a probability threshold. The lack of an
explicit requirement for an existence probability assessment and
probability threshold is likely to result in many more items meeting the**

#37

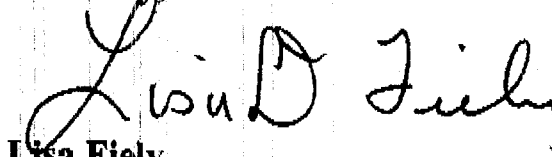
CFOC (some letters submitted separately are repeated here) - Preparer

definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,



**Lisa Fiely
Chief Financial Officer
U.S. Agency for International
Development**

#37

CFOC (some letters submitted separately are repeated here) - Preparer



August 3, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

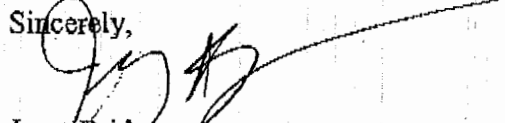
Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,



Jerry Bridges
Chief Financial Officer



1201 New York Avenue, NW ★ Washington, DC 20525
202-606-5000 ★ www.nationalservice.org

Senior Corps ★ AmeriCorps ★ Learn and Serve America

USA
Freedom Corps
The President's Call to Service
185 of 225



AUG - 7 2006

United States
Department of
Agriculture
Office of the Chief
Financial Officer
1400 Independence
Avenue, SW
Washington, DC
20250

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

Charles R. Christopherson, Jr.
Chief Financial Officer



UNITED STATES DEPARTMENT OF COMMERCE
Chief Financial Officer
Assistant Secretary for Administration
Washington, D.C. 20230

AUG - 4 2006

Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

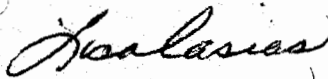
Enclosed are the Department's detailed comments to the Exposure Draft. We have significant concerns about one aspect of the proposed Concept Statement. In our response, we communicate our significant concerns about the proposed Concept Statements' dramatic expansion of the definition of a liability.

We strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, we support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

We also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, we suggest maintaining the current asset and liability definitions and including them in the proposed Concepts Statement.

We look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,



Lisa Casias
Deputy Chief Financial Officer and
Director for Financial Management

Enclosure

#37

CFOC (some letters submitted separately are repeated here) - Preparer



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE CHIEF FINANCIAL OFFICER

THE CHIEF FINANCIAL OFFICER

AUG - 9 2006

Ms. Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.S., Suite 6814
Washington, DC 20548

RE: FASAB Exposure Draft, Definition and Recognition and Measurement of Elements of
Accrual-Basis Financial Statements, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED),
Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements,
dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6
(Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions
have served us well in explicitly determining whether an item is an asset or liability for inclusion
in our agency's accrual-basis financial statements. To this end, I support the Alternative View in
Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the
current definitions, for an assessment of existence probability and a probability threshold. The
lack of an explicit requirement for an existence probability assessment and probability threshold
is likely to result in many more items meeting the definition of an element and being recognized
in the financial statements. As a result, the proposed definitions would fall short in fulfilling a
number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of
financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework)
for determining items that are elements of accrual-basis financial statements and those that are
not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest
maintaining the current asset and liability definitions and including them in the proposed Concept
Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from
the Chief Financial Officers Council. In closing, I look forward to working with you and your
staff in the future development of this Statement and others, as they become active projects.

Sincerely,

A handwritten signature in cursive script, appearing to read "Lawrence A. Warder".

Lawrence A. Warder

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:


Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,


James T. Campbell
Acting Chief Financial Officer
Department of Energy



CFOC (some letters submitted separately are repeated here)
DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of the Secretary

AUG 4 2006

Washington, D.C. 20201

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 631
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

Sheila Conley
Deputy Assistant Secretary, Finance



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-3000

CHIEF FINANCIAL OFFICER

August 3, 2006

VIA FAX: 202-208-6940

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, DC 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely

Handwritten signature of John W. Cox in black ink.
John W. Cox

#37

CFOC (some letters submitted separately are repeated here) - Preparer



U.S. Department of Justice

Washington, D.C. 20530

August 9, 2006

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW
Suite 6814
Washington, DC 20648

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed Exposure Draft. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of a probability threshold. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

#37

CFOC (some letters submitted separately are repeated here) Fed-Preparer

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

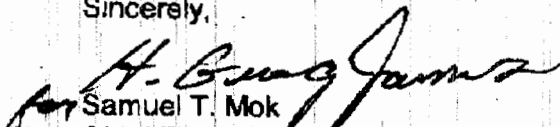
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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,


Samuel T. Mok
Chief Financial Officer
Department of Labor

**United States Department of State****Deputy Chief Financial Officer****Washington, D.C. 20520**

August 7, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our accrual-basis financial statements. Accordingly, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

Christopher H. Flaggs



CFOC (some letters submitted separately are repeated here) - Preparer

United States Department of the Interior

OFFICE OF THE ASSISTANT SECRETARY
POLICY, MANAGEMENT AND BUDGET
Washington, DC 20240



AUG 23 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

R. Thomas Weimer
Assistant Secretary



**U.S. Department of
Transportation**

Office of the Secretary
of Transportation

Assistant Secretary
for Budget and Programs
and Chief Financial Officer

400 Seventh St., S.W.
Washington, D.C. 20590

AUG - 4 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of
Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED),
*Definition and Recognition and Measurement of Elements of Accrual-Basis Financial
Statements*, dated June 7, 2006.

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threshold is likely to result in many more items meeting the definition of an element and being
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benefit) of financial reporting.

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not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest
maintaining the current asset and liability definitions and including them in the proposed
Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,

A handwritten signature in cursive script, reading "Phyllis F. Scheinberg". The signature is written in dark ink and is positioned above the printed name.

Phyllis F. Scheinberg
Assistant Secretary for Budget and Programs/CFO

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

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Sincerely,

Robert J. Henke
Robert J. Henke
Assistant Secretary, Office of Management
and Chief Financial Officer
Department of Veteran Affairs

#37

CFOC (some letters submitted separately are repeated here) - Preparer



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

AUG 15 2006

OFFICE OF
CHIEF FINANCIAL OFFICER

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

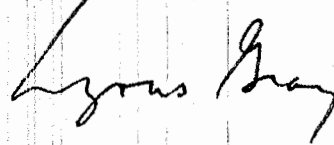
I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

#37

CFOC (some letters submitted separately are repeated here) - Preparer

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,



Lyons Gray
Chief Financial Officer
Environmental Protection Agency

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

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Robert M. Lauer
Chief Financial Officer
General Services Administration

#37

CFOC (some letters submitted separately are repeated here) - Preparer

National Aeronautics and
Space Administration

Headquarters

Washington, DC 20546-0001



August 8, 2006

Reply to Attn of: OCFO

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

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I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively at this time. The current definitions have served many agencies well in explicitly determining whether an item is an asset or liability for inclusion in the agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

A handwritten signature in cursive script, appearing to read "Terry Bowie".
Terry Bowie, CPA, CGFM
Deputy Chief Financial Officer

#37

CFOC (some letters submitted separately are repeated here) - Preparer

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

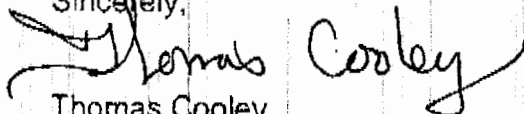
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The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.

Sincerely,



Thomas Cooley
Director of Budget, Finance and Award Management
and Chief Financial Officer
National Science Foundation

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

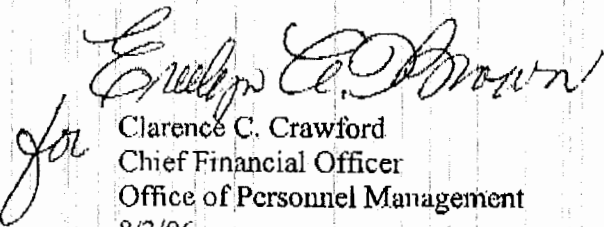
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I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.


for Clarence C. Crawford
Chief Financial Officer
Office of Personnel Management
8/3/06

#37

CFOC (some letters submitted separately are repeated here) - Preparer

U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

AUG - 9 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, N.W., Suite 6814
Washington, D.C. 20548

RE: FASAB Exposure Draft, *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006

Dear Ms. Comes:

Thank you for the opportunity to review and comment on the FASAB Exposure Draft (ED), *Definition and Recognition and Measurement of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006.

I strongly support maintaining the current asset and liability definitions in SFFAS No. 6 (Appendix E Glossary) and SFFAS No. 5 (Paragraph 19), respectively. The current definitions have served us well in explicitly determining whether an item is an asset or liability for inclusion in our agency's accrual-basis financial statements. To this end, I support the Alternative View in Appendix A of the proposed ED. This view supports the explicit requirement, as embodied in the current definitions, for an assessment of existence probability and a probability threshold. The lack of an explicit requirement for an existence probability assessment and probability threshold is likely to result in many more items meeting the definition of an element and being recognized in the financial statements. As a result, the proposed definitions would fall short in fulfilling a number of the qualitative characteristics (e.g., relevance, reliability, and cost vs. benefit) of financial reporting.

I also strongly support FASAB's current efforts to provide a common foundation (or framework) for determining items that are elements of accrual-basis financial statements and those that are not. Therefore, in strong support of FASAB's Conceptual Framework project, I suggest maintaining the current asset and liability definitions and including them in the proposed Concept Statement.

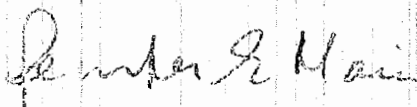
SBA IS AN EQUAL OPPORTUNITY EMPLOYER AND PROVIDER



#37

CFOC (some letters submitted separately are repeated here) - Preparer

The answers to the "Questions for Respondents" will be provided to you in a separate letter from the Chief Financial Officers Council. In closing, I look forward to working with you and your staff in the future development of this Statement and others as they become active projects.



Jennifer E. Main
Chief Financial Officer

August 22, 2006

Wendy M. Comes, Executive Director
Federal Accounting Standards Advisory Board
Mail Stop 6K17V
441 G Street, NW – Suite 6814
Washington, DC 20548

Dear Ms. Comes:

We are pleased to comment on the Proposed Statement of Federal Financial Accounting Concepts entitled *Definition and Recognition of Elements of Accrual-Basis Financial Statements*, dated June 7, 2006 (the “Exposure Draft” or the “proposed Concepts Statement”).

Our responses to the Federal Accounting Standards Advisory Board’s (FASAB’s) Questions for Respondents included in the Exposure Draft are as follows. Our answers to specific questions are in *italic*.

1. Two principles underlie the FASAB’s approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The first principle is that the definitions of assets and liabilities should derive from identifying the *fundamental or essential characteristics* that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. (See paragraphs 3, 19, 21, 40, and 49.)

- a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

Definitions of assets and liabilities should derive from the fundamental or essential characteristics that all assets and liabilities share. Use of other than those characteristics may lead to confusion as to existence and may suggest an ad hoc approach to such definitions.

- b) Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?

Definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities. Introduction of other elements diminishes the integrity of the conceptual basis of financial statements and may lead to confusion.

The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. (See paragraphs 4–6, 8, and 9.)

- c) If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.

An item that meets the definition of an asset should be considered an asset regardless of whether it is recognized in the body of the financial statement. Measurement of the asset in a manner consistent with the measurement attribute being used is a separate concept. Additionally, determining materiality requires consideration of all relevant factors.

- 2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: *assets, liabilities, net position, revenues and expenses*. (See paragraphs 2, 3, 35-37, and 56.)

- a) Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?

Assets, liabilities, net position, revenues, and expenses are the essential elements of the financial statements. Other information such as appropriations and budget-related elements may be relevant but are not essential elements of the financial statements.

Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement.

- b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

See answer to 2a. No additional elements need to be defined for the financial statements.

3. The proposed Concepts Statement addresses the government's ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services to another entity must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government's power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government's ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44. (See appendix A.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government's ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. The government's ability to change the law is inherent in sovereign powers and is effectively pervasive to all assets and obligations. To meet the definition of a liability, the government must have a present obligation. Liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. What may or may not occur in the future is information that may be relevant to financial statements but should not impact whether a present obligation exists at any point in time.

4. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to *all* federal government assets: (a) An asset embodies economic benefits or services that can be used in the future, and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities. (See paragraphs 19 and 21–34.)
 - a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

We agree that these two characteristics are essential characteristics of all federal government assets. Additionally, we believe the FASAB should consider the various types of structures that may be used and whether the concept of “control” should incorporate a risks and rewards notion, similar to the model under FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government assets?

We believe there are no additional characteristics that are fundamental or essential to all federal government assets.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are *fundamental* or *essential* to all federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity, and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur. (See paragraphs 37 and 40–48.)

- a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

We do not agree that the federal government and the other entity must have an agreement or understanding as to when settlement of the obligation is to occur. Whether or not the government is free to decide when to settle the obligation should not affect whether a liability exists. Uncertainty as to the timing of settlement would impact the measurement of the liability. The existence of a liability should be based solely on whether a present obligation exists which arose as a result of a past transaction or other event and has not yet been settled.

- b) Are there any *additional* characteristics that are *fundamental* or *essential* to all federal government liabilities?

We believe there are no additional characteristics that are fundamental or essential to all federal government liabilities.

6. As indicated in Question 1a), the first principle of the Board’s approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

- a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? (See paragraphs 17 and 38.) If not, how would you modify the definitions?

We believe the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived.

- b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? (See paragraphs 50, 52, and 53.) If not, how would you modify the definitions?

We believe the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities.

- 7. The proposed concepts statement establishes two conditions (“recognition criteria”) that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element, and (2) the item must be measurable. (See paragraphs 4 and 5.)

- a) Are there *other* criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

No. The proposed conditions are sufficient and appropriate criteria.

- 8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the *existence* of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for *recognition*, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards. (See paragraphs 7, 8, 18, and 39.)

Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including

items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

We do not agree with the position taken in the proposed Concepts Statement. The use of a probability threshold provides a mechanism to screen irrelevant items from recognition. As a practical matter, if probability is not a criterion for recognition, we have reservations about how to manage the quantity of "irrelevant" items that might need to be recognized.

9. The proposed Concepts Statement defines "measurable" as "means quantifiable in monetary units" (par. 5). The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit, and materiality and how these factors influence standard setting. (See paragraphs 57–61.)

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable ("measurability probability"), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

We are uncertain as to the FASAB's intent with regard to the requirement that the item be measurable. By measurable, does the FASAB mean that an item's value must be estimable? We understand that the value of certain types of assets owned by the federal government may not be estimable because of a complete absence of transactions that would indicate a value. If this is the FASAB's intent, we agree that an item must be measurable.

10. SFFAC 1, *Objectives of Federal Financial Reporting*, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable). (See Appendix A: Alternative Views.)

- a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

We agree with the position taken in the proposed Concepts Statement. The characteristics are implied and do not need to be repeated.

On page 29, the “expected value approach” is mentioned. This should be defined in the Glossary on page 30.

We appreciate the opportunity to comment on the Exposure Draft. If you have any questions concerning our comments, please contact Patrick Hardiman at (202) 378-5460.

Yours truly,

Deloitte & Touche LLP

August 25, 2006

Wendy Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Advancing
Government
Accountability

2208 Mount Vernon Ave
Alexandria, VA 22301

(703) 684-6931
(703) 548-9367 (fax)

Dear Ms. Comes:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments on the exposure draft (ED) of a proposed statement of Federal Financial Accounting Concepts, entitled *Definition and Recognition of Elements of Accrual-Based Financial Statements*. The FMSB, comprising 21 members with accounting and auditing backgrounds in federal, state and local government, academia and public accounting, reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately.

The FMSB has responses to the questions for respondents and some additional comments. Our responses are in bold text. The text in italics is from the FASAB document.

1. Two principles underlie the FASAB's approach to defining and recognizing elements of accrual-basis financial statements of the federal government.

The two principles identified below are not articulated as principles in the proposed ED. The two statements are not highlighted as foundational assumptions (principles) for the ED. If they rise to the level of "principles, they should be identified as such in the document.

The first principle is that the definitions of assets and liabilities should derive from identifying the fundamental or essential characteristics that all assets and liabilities, respectively, share. The definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

Does the use of the word "or" in "fundamental or essential" above imply that the 2 words are equivalent or is the word "or" meant to imply "either/or" as either "fundamental or essential?"

a) Should the definitions of assets and liabilities derive from their fundamental or essential characteristics? Please provide the reasons for your position and any alternative approach(s) you would take to define assets and liabilities.

The definitions should derive from their fundamental or essential characteristics for consistency with accounting guidance and education. (As noted, this statement is not identified as a "principle" in the ED.)

b) *Should the definitions of net position, revenues, and expenses derive from the definitions of assets and liabilities? Please provide the reasons for your position and any alternative approach(s) you would take to define net position, revenues, and expenses?*

Yes, we think that this position is logical and reasonable.

*The second principle is that definition and recognition are separate concepts. An item that meets the definition of an asset is an asset but to be recognized the asset also must meet the recognition criteria. Thus, meeting the definition of an element is a necessary but not a sufficient condition for an item to be recognized in financial statements. An asset that is not recognized in the body of a financial statement would be a candidate for disclosure in the notes. **The ED mentions several times that assets or liabilities not recognized in the body of the financial statements would be “a candidate for disclosure in the notes or in supplemental information. Should the ED discuss how the decision to disclose should be made?”***

c) *If an item meets the definition of an asset is it an asset even if it is not recognized in the body of a financial statement because, for example, it is not measurable or its amount is not material? Please provide the reasons for your position.*

We agree that an asset can be defined as an asset without being sufficiently measurable or material to be in the body of the financial statement. Having said that, we think it would be helpful if the ED provided more examples of assets that may not be sufficiently measurable or material to be in the body of the financial statement.

In summary, we agree with the two statements, but recommend that the ED clearly articulate that these are principles and foundational assumptions of the ED; they appear to be logical and workable.

*2. The proposed Concepts Statement defines five elements of accrual-basis financial statements: assets, liabilities, net position, revenues and expenses. **The proposed ED can’t seem to “make up its mind” about whether “net position” is an element. Net position is not mentioned in paragraph 2 or paragraph 9 which “identify” the elements. The other references noted in this question (e.g., paragraphs 35-37 and 56) do not really define the elements; they refer to a limited number of the elements.***

a) *Are there additional elements of accrual-basis financial statements that should be defined in the Concepts Statement? If so, what are they and what are their essential characteristics? Alternatively, what are they and how would you define them?*

The only additional elements that should be defined might be “gains or losses” as discussed below.

*Some constituents believe that because of the unique nature of the federal government additional elements are needed for certain transactions and other events. For example, certain intangible resources, long-term social obligations, and other commitments are viewed by these constituents as requiring a different element or elements than those identified in this proposed Concepts Statement. **The ED does not discuss these beliefs so that we cannot judge whether they are realistic or valid.***

b) Do you agree or disagree that there are additional elements that need to be defined? If you agree, what are the essential characteristics of these elements? Please provide examples of the types of transactions that align with these additional elements.

An additional element could be “gains or losses”. Paragraphs 55 and 56 make the point that “gains or losses” are merely sub-sets of revenues and expenses. However, in most cases, gains or losses are not reported as either revenues or expense. Gains or losses represent a composite entry on financial statements, generally the net result of a transaction primarily affecting assets or liabilities. The gain or loss is the “remainder” of such a transaction. For example, if an entity sells an asset at less than recorded value – it records a loss. Conversely, if it sells an asset at more than recorded value it records a gain. However, the entity does not record the receipt of cash as revenue and the value of the underlying asset as an expense. Thus, the gain or loss is not a subset or revenues and expenses – it is the result of an asset or liability transaction and thus could be considered as another element.

3. The proposed Concepts Statement addresses the government’s ability to change laws in the future as stated in paragraph 44 as follows:

To meet the definition of a liability, the federal government’s contract or other agreement to provide assets or services to another entity must be based on existing conditions, including current law, because an essential characteristic of a liability is that the government has a present obligation, even if conditions may change before settlement is due. For example, the Congress may change a law under which the federal government has incurred a present obligation and erase the obligation or otherwise enable the government to avoid settlement. Alternatively, the government may be able in the future to renegotiate the obligation with the payee or recipient of the promised services. However, liabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government’s power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

Members with an alternative view believe that the government’s power to modify the law to change or withdraw future benefits related to nonexchange transactions could affect the existence of a present obligation. Consequently, these Board members believe that the government’s ability to change the law may provide additional evidence about whether a present obligation exists and, in some instances, may preclude recognition of a liability. Therefore, they disagree with paragraph 44.

a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the potential effect of the government’s ability to change laws on the recognition of a liability? Please explain the reasons for your position.

We agree with the proposed Concept Statement (1). The existence or non-existence of a liability should be based on the law at the time. Congress can always modify legislation in a way that will affect the existence of liabilities (or assets). If and when that happens the financial statements should be modified with appropriate disclosure of the reasons for the changes in the financial statements. Law takes precedence over accounting rules and regulations, and one takes the action(s) necessary to abide by the law. It is not reasonable to second guess or predict what law(s) will change. Therefore, we agree with the position as stated in the ED, since it is the realistic approach. An example of where the government could change the law and cause a change in the liability recognition follows. The DoD accounts for environmental clean-up of its ranges under current law requiring clean up to a specified depth, three feet below the surface. There are

Members of Congress who would like to see the law changed and the depth of the clean-up increased to, say, nine feet below the surface. This would dramatically impact the clean-up costs and the liability that the DoD would have to accrue.

We also wish to point out that the AV relates only to non-exchange transactions. Can not the federal government change the law so as to affect liabilities arising from exchange transactions? Also, since the AV is the only mention of non-exchange transactions, is it necessary for the ED to define exchange and non-exchange transactions?

4. The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government assets: (a) An asset embodies economic benefits or services that can be used in the future and (b) the government can control access to the economic benefits or services and therefore, can obtain them and deny or regulate the access of other entities.

This is not the definition of an asset per paragraph 17. That paragraph says that “an asset is a resource that embodies economic benefits or services that the government can control”. That definition does not embody the concept of future benefits. Other references to the definition are mixed about embodying the concept of future benefits – for example, see the Executive Summary, the Glossary, paragraphs 21, 22, 25. We recommend that each mention of economic benefits or services refer to “future” economic benefits or services.

a) Do you agree that these two characteristics are essential characteristics of all federal government assets? If not, please give an example of a resource that you believe is an asset but does not possess one or both of these characteristics.

We think the two characteristics are reasonable. Statement of Financial Accounting Concepts (SFAC) #6 states that, “Assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.” If the entity (i.e., the government) does not have control of the asset, it would be difficult to claim it as an asset. Also, if the second part of the definition is removed, it may open up the financial statements to additional “assets”. At present, we cannot think of what those assets might be, but having the control characteristic in the guidance limits potential “frivolous” assets to be considered.

b) Are there any additional characteristics that are fundamental or essential to all federal government assets?

Not that we can think of.

5. The proposed Concepts Statement identifies two, and only two, characteristics that are fundamental or essential to all federal government liabilities: (a) A liability is a present obligation to provide assets or services to another entity and (b) the federal government and the other entity have an agreement or understanding as to when settlement of the obligation is to occur.

a) Do you agree or disagree that these two characteristics are essential characteristics of all federal government liabilities? Please provide the reasons for your views. If you disagree, please give an example of an obligation or commitment that you believe is a liability but does not possess one or both of these characteristics.

SFAC #6 state that, “Liabilities are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.” We think both parts of the definition are necessary. If the federal government has a liability, but there is no “due date” or no action that will precipitate a due date, in essence the government does not have a liability.

b) Are there any additional characteristics that are fundamental or essential to all federal government liabilities?

Not that we can think of.

6. As indicated in Question 1a), the first principle of the Board’s approach to defining elements is that the definitions of assets and liabilities should derive from their essential characteristics, and the definitions of net position, revenues, and expenses should derive from the definitions of assets and liabilities.

a) Do the definitions of assets and liabilities adequately convey the essential characteristics from which they are derived? If not, how would you modify the definitions?

Yes.

b) Do the definitions of net position, revenues, and expenses adequately convey their relationship to assets and liabilities? If not, how would you modify the definitions?

Yes. Conceptually, we believe the definitions convey the essential characteristics. We also suggest that “gains and losses” should be a separate element – see above.

7. The proposed concepts statement establishes two conditions (“recognition criteria”) that should be met for an item to be recognized in the body of a financial statement: (1) The item must meet the definition of an element and (2) the item must be measurable.

a) Are there other criteria that should be established as conditions for recognition? If so, what recognition criteria would you add or delete?

No. We have no other proposed criteria.

8. The proposed Concepts Statement neither explicitly requires nor precludes an assessment of probability when deciding whether an item meets the definition of an element, nor does the Statement establish an explicit threshold of probability at the definition stage. Rather, the Statement indicates that conclusions about the existence of an element require judgment as to whether, based on the available evidence, an item possesses the essential characteristics of an element. The Statement indicates that when an element is considered for recognition, measurement of the element may require an assessment of the probability of future inflows or outflows of resources to or from the element to enhance the reliability of amounts recognized in the financial statements. In addition, the Statement explicitly acknowledges that assessments of the materiality and benefit versus cost of recognizing the results of the measurement of elements may constrain recognition. Members believe that this framework permits future standard setters to adequately address uncertainty with respect to recognition decisions in establishing future standards.

*Members with an Alternative View believe that, in deciding whether an item meets the definition of an element and considering related uncertainties, there is implicitly an assessment of the probability of whether an item meets the definition of an element and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not meet the definition of an element. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item meets the definition of an element should be assessed as part of determining whether an item meets the definition of an element (“existence probability”), and (2) there exists a threshold where such probability is so low that an item would not meet the definition of an element. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for an existence probability assessment and a probability threshold at the definition stage would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities. **It would be helpful if the proponents of the AV provided examples of the types of items that may be recognized that have a low probability of being assets or liabilities.***

a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a related probability threshold when determining whether an item meets the definition of an element? Please explain the reasons for your position.

It seems to us that the proposed ED adequately addresses the need for judgment in determining the existence of an asset or liability and the amount of such asset or liability. As stated in the AV, the need for an assessment and a threshold is implicit in the ED. We are concerned that if the ED explicitly requires an assessment and a threshold, preparers would be “forced” by auditors to specifically examine and document the existence and value of each asset and liability separately from the ordinary course of business. When there is a significant question about existence or value of an asset, such documentation is appropriate. However, new and separate documentation should not be required. Therefore, while we do not have a major problem with explicitly stating the need for such an assessment, we prefer the ED to imply the need (as written) with any explicit requirements included in separate standards as required.

9. The proposed Concepts Statement defines “measurable” as “means quantifiable in monetary units.” (par. 5) The proposed Concepts Statement does not explicitly discuss an assessment of probability when deciding whether, based on the available evidence, an item is measurable or that there is a point or threshold at which an item is not measurable. The Statement does discuss the consideration of uncertainty, cost-benefit and materiality and how these factors influence standard setting.

Members with an Alternative View believe that, in deciding whether an item is measurable and considering related uncertainties, there is implicitly an assessment of the probability of whether an item is measurable and that, because there is a decision to be made, that there is implicitly a probability threshold where an item would not be measurable. These members believe that the proposed Concepts Statement should explicitly state that (1) the probability that an item is measurable should be assessed as part of determining whether an item is measurable (“measurability probability”), and (2) there exists a threshold where such probability is so low that an item would not be measurable. Thresholds to be applied would, as appropriate, be established in specific standards. In the view of these members, the lack of an explicit acknowledgement of the need for a measurability probability assessment and a probability threshold would be likely to result in many more items being recognized in the financial statements, including items with a low probability of being assets or liabilities.

a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for an explicit requirement for an assessment of probability and a probability threshold when determining whether an item is measurable? Please explain the reasons for your position.

As per our response to question 8, it seems that the position taken in the proposed concepts statement is most appropriate. Again, we would appreciate more examples from the authors of the AV of items that could be added to the financial statements if the need for assessment is not explicit.

10. SFFAC 1, Objectives of Federal Financial Reporting, par. 156, states that “Financial reporting is the means of communicating with those who use financial information. For this communication to be effective, information in financial reports must have these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.” These six characteristics are defined in SFFAC 1 and are not altered by this Statement. Members supporting the proposed Concepts Statement do not believe that repeating the qualitative characteristics in this Statement would be useful and doing so could cause confusion regarding the status and application of the characteristics. These members believe that if the application of the characteristics requires explanation, the explanation should be approached in a comprehensive manner.

The members expressing an alternative view point out that the proposed Concepts Statement does not include a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria. Members with an alternative view believe that the ED should require a consideration of all of the qualitative characteristics of financial reporting in determining whether an item meets the recognition criteria; i.e., meets the definition and is measurable. In the view of these members, the lack of a consideration of the qualitative characteristics in determining whether an item meets the recognition criteria will likely result in the recognition of items that do not meet the qualitative characteristics (e.g., not relevant or reliable.)

a) Do you agree with the position taken in (1) the proposed Concepts Statement or (2) the Alternative View concerning the need for a consideration of the qualitative characteristics of financial statements as part of determining whether an item meets the recognition criteria? Please explain the reasons for your position.

We agree with the proposed Concepts Statement (1). As noted above, we have no problems with general statements that qualitative characteristics be considered, but see no real “need” to place that statement in this standard. In addition, we would like to see examples of the types of items that might be included as assets or liabilities if the qualitative factors are not considered.

Additional Comments

Paragraph 6 – recommend giving example or two (maybe in a footnote) where an item is measurable but still does not meet definition of an element and thus should be excluded.

Paragraphs 7 and 8 – the incorporation of the judgment concept as opposed to certainty and the concept of materiality and benefit versus cost are good ones.

We do not see the relevance of the entire section on “Entity Concept” in this ED. We suggest that paragraphs 10 to 16 be eliminated. The only value to be obtained from these paragraphs is that

the term “entity” includes individuals (paragraph 16), and if these paragraphs were to be eliminated, the definition of “entity” could easily be placed elsewhere in the ED.

Paragraph 36 – We recommend giving an example within this paragraph for the purpose of (1) clarity and (2) consistency with previous paragraphs where examples are provided for clarification. Such examples greatly enhance reader understandability. In addition, we suggest adding examples in paragraph 24, 29, 36 and 37 and throughout the Alternative View.

The Executive Summary is not consistent with the ED. For example, the ED does not refer to future benefits from assets. The ED also says that “measurement of an item would include an assessment of the probability of future flows of resources or services from an item”, we don’t think the ED has that requirement. In fact, such a statement in the ED is what the authors of the AV are seeking. The Exec Summary also says that the “Concepts Statement would (emphasis added) include a discussion of the effects of uncertainty....” It probably should say “Concepts Statement includes”

The ED seems to vacillate between discussing and defining “elements” or “items which make up a element” For example, paragraph 2 says “This Statement focuses on the broad classes (e.g., the elements) and their characteristics instead of defining particular assets, liabilities or other items” Paragraph 4 also relates recognition to “recording or incorporating an element into the financial statements” Then paragraph 5 goes on to discuss “recognition criteria are the conditions an item (emphasis added) should meet” The ED should be consistent in whether it is referring to an “element” or an “item.”

We are not sure that the example in paragraph 2 is relevant since the federal government does not claim that outer space is a federal asset.

Paragraph 28, we suggest that the sentence starting “In exercising control” should also include the concept that the federal government can fulfill its responsibilities to provide services to the public (as in free parks, museums, etc.)

We suggest that the word “obligation” not be used to describe a liability. While the ED tries to clarify that the word is not being used in its budgetary sense (footnote 6), there is a significant opportunity to misread the word “obligation” as a budgetary term. Perhaps the word “responsibility” can be used in lieu of “obligation”.

We are concerned with the definitions of revenues and expenses in that both exclude borrowing (receipts and repayments) in the respective definitions. The ED does not discuss why borrowing is excluded or how borrowing is to be treated. We assume that borrowing is excluded from the definitions of revenues and expenses since borrowing represents only changes in assets and liabilities. However, many other transactions represent changes in just assets and liabilities but those transactions are not excluded for the definition of revenues and expenses (for example, sale of an asset, paying invoices from a vendor (unless that is “borrowing”). More discussion of why borrowing is excluded may be appropriate.

We are also concerned about the definitions of revenues and expenses since it is unclear how accruals for things like bad debts will be handled. The definition of revenue is “an increase in assets, a decrease in liabilities or a combination of both from providing good and services, levying taxes or other impositions, receiving donations or any other activity performed during the

reporting period.” (The definition of expenses is similar.) However, an accrual for bad debts (for example) does not fall into any of these categories, unless that accrual is considered a valuation issue.

Paragraph 57 is unclear about its impact and effect.

The example in footnote 12 seems to be a contingent liability for which there are adequate standards and therefore does not require additional discussion in this ED.

No members of the FMSB objected to the issuance of this comment letter. We would be pleased to discuss this letter with you at your convenience. You can contact me at hintonrw@audits.state.ga.us or (404) 656-2174 or Anna D. Gowans Miller, CPA, AGA’s Technical Manager and facilitator for this project, at amiller@agacgfm.org or (703) 684-6931, ext. 313.

Sincerely,

A handwritten signature in black ink, appearing to read "Russell W. Hinton". The signature is stylized with a large, sweeping initial "R" and a long, horizontal flourish at the end.

Russell W. Hinton, CGFM, Chair,
AGA Financial Management Standards Board

cc. Jeffrey S. Hart, CGFM, CFE
AGA National President

**Association of Government Accountants
Financial Management Standards Board**

July 2006 – June 2007

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